

ABC ON THE BOOKS AND IN THE COURTS:  
AN ANALYSIS OF RECENT INDEPENDENT CONTRACTOR AND  
MISCLASSIFICATION STATUTES

ANNA DEKNATEL AND LAUREN HOFF-DOWNING\*

*Across the country, employers frequently misclassify workers as independent contractors, avoiding obligations to pay minimum wages and overtime, as well as unemployment, payroll, workers' compensation, and Social Security taxes. Marking employees as independent contractors not only harms workers, but also shrinks states' coffers and burdens businesses that comply with the law. In recent years, states have responded to reports of widespread misclassification by passing stricter legislation. From 2004 to 2012, twenty-two states have modified their statutory definitions of independent contractors or transformed penalties for the misclassification of employees. While prior articles have analyzed the shortcomings of existing independent contractor definitions and enforcement mechanisms, this Article is the first to offer a full analysis of the shape and effectiveness of this recent wave of corrective legislation.*

*The Article first analyzes these statutes, identifies shared and distinct features, and evaluates their strengths and weaknesses. It next examines how these statutes are faring in practice in terms of employer attempts to skirt these laws and courts' responses. Although the reforms often improve prior statutes, we identify common flaws revealed during adjudication. To avoid liability under stricter misclassification statutes, employers have used tactics such as classifying workers as business entities, exploiting subcontracting structures, and simply arguing semantic distinctions under the independent contractor tests.*

*Finally, the Article uses its analysis of current reforms and enforcement efforts to make recommendations for legislatures and courts interested in effectively limiting misclassification. Our findings suggest that the most common independent contractor definition, the "ABC" test, can successfully combat misclassification and some egregious employer tactics. Its succinct and objective demands are most effective when applied uniformly to all workers and universally across all employment statutes. However, some employers have still evaded liability under the ABC test. We provide model legislative reforms and identify arguments that plaintiffs and enforcement agencies can use to prevent employers from exploiting statutory weaknesses.*

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## INTRODUCTION

The power of the Internal Revenue Service’s 1099 form for any individual worker is vast: when an employer uses a 1099 form to file a payment, it categorizes that worker as an “independent contractor” rather than as an “employee”<sup>1</sup> and determines whether she is entitled to a vast array of legal protections and benefits.<sup>2</sup> Employees are shielded by antidiscrimination

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\* Lauren Hoff-Downing and Anna Deknatel graduated from the University of Pennsylvania Law School in 2014, where they were both Toll Public Interest Scholars. Lauren Hoff-Downing is currently a fellow at Murphy Anderson PLLC, a union and employee-side firm. Anna Deknatel is a law clerk at the Eastern District of New York Bankruptcy Court.

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<sup>1</sup> See *Reporting Payments to Independent Contractors*, IRS, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Reporting-Payments-to-Independent-Contractors> (last updated Dec. 18, 2014) (describing the use of form 1099-MISC for reporting payments to independent contractors).

<sup>2</sup> See Drew Hintze, *The Misclassification Initiative: Colorado Partners with the United States Department of Labor in an Effort to Crackdown on the Misclassification of Employees as Independent Contractors*, DULR ONLINE (Apr. 23, 2012 4:31 PM), <http://www.denverlawreview.org/online-articles/2012/4/23/the-misclassification-initiative-colorado-partners-with-the.html> (explaining that misclassification of employees as independent contractors deprives employees of benefits).

laws,<sup>3</sup> wage and hour laws, and family and medical leave protections; independent contractors are not.<sup>4</sup> Employees can access federal and state programs, including unemployment insurance and workers' compensation; independent contractors cannot.<sup>5</sup> In turn, employers are subject to liability and tax and benefit contribution requirements under these laws only for their employees.<sup>6</sup>

Thus, by misclassifying workers as independent contractors, employers avoid these obligations. The stakes are clear and high. Whether at the local or federal level, reformers have consistently identified three harms that result from misclassification. First, misclassified workers are deprived of workplace protections and remedies to workplace harms like discrimination and wage theft.<sup>7</sup> Second, businesses that play by the rules compete with businesses taking unfair advantages to their bottom line by skirting taxes.<sup>8</sup> And finally, state and local governments and their constituents are divested of millions of dollars in lost payments to unemployment insurance funds, payroll taxes, and workers' compensation funds.<sup>9</sup>

Still, until recently, many employers regularly flaunted the national and local laws governing this consequential distinction, while regulators and agencies generally looked the other way: a 2000 Department of Labor study that audited businesses in nine states indicated that between ten and thirty percent of employers misclassified at least some portion of their workers.<sup>10</sup> However, state legislators and regulators have since fiercely attacked this rampant culture of misclassification. In the last several years, over twenty states have tightened requirements on which workers can be deemed independent contractors or have instituted new and stronger punishments for those businesses that misclassify.<sup>11</sup> Burdens on local government coffers appear

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<sup>3</sup> Coverage, U.S. EQUAL OPPORTUNITY EMP'T COMM'N, <http://www.eeoc.gov/employers/coverage.cfm> (last visited Jan. 22, 2015).

<sup>4</sup> Hintze, *supra* note 2; Wage and Hour Div., U.S. Dep't of Labor, *Employee Misclassification as Independent Contractors*, U.S. DEPARTMENT OF LABOR, <http://www.dol.gov/whd/workers/misclassification/> (last visited Jan. 22, 2015).

<sup>5</sup> Hintze, *supra* note 2; Wage and Hour Div., *supra* note 4.

<sup>6</sup> See, e.g., Hintze, *supra* note 2 (explaining that employers who misclassify workers do not pay "federal and state unemployment taxes, Social Security and Medicare taxes, and workers' compensation benefits"); Wage and Hour Div., *supra* note 4 ("Employee misclassification also generates substantial losses to the Treasury and the Social Security and Medicare funds, as well as to state unemployment insurance and workers compensation funds.").

<sup>7</sup> Robert W. Wood, *New Age Scrutiny of Employee vs. Contractor Liabilities*, 2009 BUSINESS LAW NEWS, THE STATE BAR OF CALIFORNIA, no. 2, at 12, 12 (An employer "must pay [employees] wages, withhold taxes, give them employee benefits, be liable for any acts of negligence during their employment, and face the scrutiny of state and federal law when it comes to nondiscrimination, discipline, and termination.").

<sup>8</sup> Olympia Meola, *Va. Should Consider Outlawing Misclassifying Workers*, JLARC Says, TIMESDISPATCH.COM (June 11, 2012, 4:11 PM), <http://www2.timesdispatch.com/news/virginia-politics/2012/jun/11/va-should-consider-outlawing-misclassifying-worker-ar-1979801/>. "Employers who are correctly categorizing may not have a 'level playing field,' said JLARC [Joint Legislative Audit and Review Commission] project leader Walt Smiley." *Id.*

<sup>9</sup> Chaz Bolte, *Triple Jeopardy: Misclassification Doesn't Just Cost Workers Wages, It Robs Government of Revenue and Local Business of a Chance to Compete*, WEPARTYPATRIOTS.COM (Dec. 8, 2011), <http://wepartypatriots.com/wp/2011/12/08/misclassification-epidemic/>.

<sup>10</sup> PLANMATICS, INC., INDEPENDENT CONTRACTORS: PREVALENCE AND IMPLICATIONS FOR UNEMPLOYMENT INSURANCE PROGRAMS, at iii (2000), <http://wdr.doleta.gov/owsdrr/00-5/00-5.pdf>; see also U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-09-717, EMPLOYEE MISCLASSIFICATION: IMPROVED COORDINATION, OUTREACH, AND TARGETING COULD BETTER ENSURE DETECTION AND PREVENTION 11 (2009), <http://www.gao.gov/assets/300/293679.pdf>.

<sup>11</sup> See An Act Further Regulating Public Construction in the Commonwealth, 2004 Mass. Legis. Serv. ch.

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139 (West) (codified as amended in scattered sections of MASS. GEN. LAWS ANN. (West 2004)) (effective July 19, 2004); Act of April 4, 2005, 2005 N.M. Laws ch. 94, (codified at N.M. STAT. ANN. § 60-13-3.1 (West 2005)) (effective June 17, 2005); An Act Relating to Independent Contractors, 2005 Or. Laws ch. 533 (West) (codified as amended at OR. REV. STAT. ANN. §§ 310.800, 316.162, 670.600, 670.605, 657.040 (West 2006)) (effective Jan. 1, 2006); Act of May 25, 2007, 2007 Minn. Sess. Law Serv. ch. 135 (West) (codified as amended in scattered sections of MINN. STAT. ANN. (West 2007)); An Act Concerning Penalties for Concealing Employment or Other Information Related to Workers' Compensation Premiums, 2008 Conn. Legis. Serv. P.A. 07-89 (West) (codified as amended at CONN. GEN. STAT. ANN. §§ 31-288, 31-69a, 31-76a (West 2007)); Construction Industry Independent Contractor Act, 2007 N.J. Sess. Law Serv. ch. 114 (West) (codified at N.J. STAT. ANN. §§ 34:20-1 to 34:20-11 (West 2007)) (effective July 13, 2007); Act of July 17, 2007, 2007 N.H. Adv. Legis. Serv. ch. 362 (LexisNexis) (codified as amended at N.H. REV. STAT. ANN. §§ 275:4, 275:42, 275-E:1, 279:1, 281-A:2, 6:12 (2012)) (effective Jan. 1, 2008); Employee Classification Act, 2007 Ill. Laws 26 Legis. Serv. ch. 26 (West) (codified at 820 ILL. COMP. STAT. ANN. 185/1 to 185/999 (West 2007)) (effective Jan. 1, 2008); Act of Mar. 20, 2008, 2008 Wash. Legis. Serv. ch. 102 (West) (codified as amended at WASH. REV. CODE ANN. §§ 50.04.145, 51.08.070, 51.08.180, 51.08.181, 51.08.195 (West 2008)) (effective June 12, 2008); An Act Concerning Employee Misclassification, 2008 Conn. Legis. Serv. P.A. 08-156 (West) (codified at CONN. GEN. STAT. ANN. §§ 31-57h, 31-57i (West 2008)) (effective July 1, 2008); An Act Concerning the Misclassification of Employers as Independent Contractors, 2009 Colo. Sess. Laws ch. 406 (codified at COLO. REV. STAT. ANN. § 8-72-114 (2009)) (effective June 2, 2009); Act of July 28, 2009, 2009 Or. Laws ch. 845 (West) (codified at OR. REV. STAT. ANN. §§ 670.700, 670.705 (West 2009)) (effective July 1, 2009); An Act to Ensure that Construction Workers Are Protected by Workers' Compensation Insurance, 2009 Me. Legis. Serv. ch. 452 (West) (codified as amended at ME. REV. STAT. ANN. tit 26, §§ 1302-A, 1312, tit. 39-A, §§ 102, 105-A (2009)) (effective Sept. 12, 2009); Workplace Fraud Act of 2009, 2009 Md. Code Ann. Adv. Legis. Serv. ch. 188 (LexisNexis) (codified as amended in scattered sections of MD. CODE ANN., LAB. & EMPL. (LexisNexis 2009)) (effective Oct. 1, 2009); Workplace Fraud Act, 77 Del. Laws ch. 192 (2009) (codified at DEL. CODE ANN. tit. 19, §§ 3501-3514 (West 2009)) (effective Oct. 29, 2009); An Act to Amend the Indiana Code Concerning Labor and Safety, 2009 Ind. Legis. Serv. ch. 164 (West) (codified at IND. CODE ANN. §§ 6-8.1-3-21.2, 22-1-1-22, 22-3-1-5, 22-4.1-4-4 (West 2010)) (effective Jan. 1, 2010); Act of March 25, 2010, 2010 Ind. Legis. Serv. P.L. 110-2010 (West) (codified as amended in scattered sections of IND. CODE ANN. (West 2010)) (effective July 1, 2010); An Act Relating to Misclassification of Employees to Lower Premiums for Workers' Compensation and Unemployment Compensation, 2010 Vt. Legis. Serv. ch. 142 (West) (codified as amended in scattered sections of VT. STAT. ANN. (West 2010)) (effective July 1, 2010); An Act To Amend the Laws Governing the Misclassification of Construction Workers, 2010 Me. Legis. Serv. ch. 649 (West) (codified as amended at ME. REV. STAT. ANN. tit. 39-A, § 105-A (2010)) (effective July 12, 2010); Employee Classification Act, 2010 Neb. Laws ch. 563 (codified at NEB. REV. STAT. ANN. §§ 48-2901 to 48-2912 (LexisNexis 2010)) (effective July 15, 2010); An Act Implementing the Recommendations of the Joint Enforcement Commission on Employee Misclassification, 2010 Conn. Legis. Serv. P.A. 10-12 (West) (codified as amended at CONN. GEN. STAT. ANN. §§ 31-69a, 31-288 (West 2010)) (effective Oct. 10, 2010); New York State Construction Industry Fair Play Act, 2010 N.Y. Sess. Laws ch. 418 (McKinney) (codified at N.Y. LAB. LAW §§ 861 to 861-f (McKinney 2010)) (effective Oct. 26, 2010); Act of May 12, 2010 2009 Wis. Legis. Serv. ch. 292 (West) (codified at WIS. STAT. ANN. §§ 103.005(10), 103.06 (West 2011)) (effective Jan. 1, 2011); Construction Workplace Misclassification Act, 2010 Pa. Legis. Serv. ch. 72 (West) (codified at 43 PA. STAT. ANN. §§ 933.1-933.17 (West 2011)) (effective Feb. 10, 2011); Worker Classification Coordinated Enforcement Act, 2011 Utah Laws ch. 15 (codified at UTAH CODE ANN. §§ 34-47-101 to 34-47-202 (LexisNexis 2011)) (effective Mar. 7, 2011); Construction Licensees Related Amendments, 2011 Utah Laws ch. 413 (codified as amended in scattered sections of UTAH CODE ANN. (LexisNexis 2011)) (effective July 1, 2011); Act of May 12, 2011, 2011 Kan. Sess. Laws ch. 81 (codified as amended at KAN. STAT. ANN. §§ 44-703, 44-766, 79-3234 (West 2011)) (effective July 1, 2011); An Act Concerning Independent Contractors in the Trucking and Messenger Courier Industries, 2011 Me. Legis. Serv. ch. 176 (West) (codified at ME. REV. STAT. ANN. tit. 39-A § 114 (2011)) *repealed by* An Act to Standardize the Definition of "Independent Contractor," 2012 Me. Legis. ch. 643 (West 2012); Act of Oct. 9, 2011, 2011 Cal. Legis. Serv. ch. 706 (West) (codified at CAL. LAB. CODE §§ 226.8, 2753 (West 2012)) (effective Jan. 1, 2012); Act of May 2, 2012, 2012 Md. Code Ann. Adv. Legis. Serv. ch. 206 (LexisNexis) (codified as amended at MD. CODE ANN., LAB. & EMPL. §§ 3-903, 3-903.1, 3-905, 3-906, 3-913 (LexisNexis 2012)) (effective July 1, 2012); Act of May 31, 2012, 2012 Kan. Sess. Laws ch. 166 (codified as amended in scattered sections of KAN. STAT. ANN. (West 2012)) (effective July 1, 2012); An Act to Standardize the Definition of "Independent Contractor," 2012 Me. Legis. ch. 643

to have ignited this wave of statutory change. The economic recession beginning around 2007 collapsed state tax revenues and triggered budget gaps in states across the country.<sup>12</sup> Simultaneously, demand for safety net services including unemployment insurance rose steeply, driving some state unemployment trust funds to insolvency at exactly the moment states had no extra cash flow.<sup>13</sup>

The scale of these shortfalls varied by state and was inevitably shaped by each state's size, industries, prior legal standards, and enforcement practices, but the issue has not discriminated by region. Around the country, academic and government reports have measured the impact of misclassification on state tax revenues or unemployment insurance funds and found sizeable deficits.<sup>14</sup> For example, Colorado's labor and employment agency assessed that an imposing \$167 million in income tax revenue had gone unpaid annually between 2009 and 2010.<sup>15</sup> A policy center focused on Maine's construction industry estimated its state income tax shortfall for the construction industry alone could be as high as \$4.3 million per year.<sup>16</sup> An analysis of 2002 to 2005 audits of the New York Department of Labor's Unemployment Insurance Division revealed an annual average of more than \$175 million in underreported taxes to the state's unemployment insurance fund.<sup>17</sup> Additionally, a state-funded task force in Maryland estimated that the state had lost as much as \$20 million in contributions to its trust fund annually.<sup>18</sup>

States have since set out to collect these lost dollars. Unlike other budget balancing tactics, such as tax increases or service reduction, enforcing and strengthening misclassification laws appear to have garnered broad political support. Unions have emphasized that reform can protect workers and provide access to benefits;<sup>19</sup> construction workers were vocal during a

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(West) (codified at ME. REV. STAT. ANN. tit. 1, § 1012, tit. 5, § 19, tit. 26, §§ 591, 591-A, 1043, tit. 39-A, §§ 102, 105-A, 401 (2012)) (effective Dec. 31, 2012).

<sup>12</sup> See Tracy Gordon, *State and Local Budgets and the Great Recession*, BROOKINGS INSTITUTION (Dec. 2012), <http://www.brookings.edu/research/articles/2012/12/state-local-budgets-gordon> ("Figure 3 shows that these receipts fell by roughly \$100 billion in real terms from 2007 to 2009.")

<sup>13</sup> See *id.* ("Figure 5 shows that caseloads for public programs indeed continued or escalated in the downturn. In particular, enrollments climbed for Medicaid, Unemployment Insurance, and higher education from 2007 to 2009."); Sarah Leberstein, Nat'l Emp't Law Project, *Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries*, Nat'l Emp't Law Project 3 (updated Aug. 2012), [http://nelp.3cdn.net/0693974b8e20a9213e\\_g8m6bhyfx.pdf](http://nelp.3cdn.net/0693974b8e20a9213e_g8m6bhyfx.pdf).

<sup>14</sup> Leberstein, *supra* note 13.

<sup>15</sup> COLO. DEP'T OF LABOR AND EMP'T, MISCLASSIFICATION OF EMPLOYEES AS INDEPENDENT CONTRACTORS, ANNUAL COMPLIANCE REPORT 11 (2011), <http://www.colorado.gov/cs/Satellite?blobcol=urldata&blobheader=application/pdf&blobkey=id&blobtable=MungoBlobs&blobwhere=1251719071697&ssbinary=true>.

<sup>16</sup> FRANÇOISE CARRÉ & RANDALL WILSON, CONSTRUCTION POLICY RESEARCH CENTER, THE SOCIAL AND ECONOMIC COSTS OF EMPLOYEE MISCLASSIFICATION IN THE MAINE CONSTRUCTION INDUSTRY 2, 10-11 (2005), <http://www.law.harvard.edu/programs/lwp/Maine%20Misclassification%20Maine.pdf>.

<sup>17</sup> LINDA H. DONAHUE, JAMES RYAN LAMARE & FRED B. KOTLER, CORNELL UNIV., THE COST OF WORKER MISCLASSIFICATION IN NEW YORK STATE 10 (2007), <http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1009&context=reports>.

<sup>18</sup> MD. DEP'T OF LABOR, LICENSING AND REGULATION, ANNUAL REPORT OF THE JOINT ENFORCEMENT TASK FORCE ON WORKPLACE FRAUD 6 (2009), <http://www.dllr.state.md.us/workplacefraudtaskforce/wpftfannrep.pdf>.

<sup>19</sup> See *Teamsters Support Senate Efforts To Protect Workers From Misclassification*, Teamsters (June 17, 2010), <http://teamster.org/content/teamsters-support-senate-efforts-protect-workers-misclassification>.

Vermont legislative campaign,<sup>20</sup> and a carpenters union fought for reform in Minnesota and Wisconsin.<sup>21</sup>

In particular, advocates have successfully prevented mass resistance to these reform measures by labeling resistance “job killing” or harmful to business, and by highlighting benefits of more effective regulatory schemes to businesses that follow the law. As Ellen Golombek, Executive Director of the Colorado Department of Labor and Employment, succinctly explained, misclassification “destabilizes the business climate by causing responsible businesses to suffer unfair competition.”<sup>22</sup> States increasing penalties for violating existing definitions of independent contracting have especially seen support from some members of their business community, as the costs of stricter enforcement of the legal status quo would only be borne by current rule breakers.<sup>23</sup>

In some states, prior legal regimes were themselves complex, making compliance costly and acting as a barrier to the legitimate use of independent contracting, which can be beneficial to both businesses and the people they hire. As one example, Oregon’s legislature was motivated by a mobilized business community calling for “an easier to understand and more broadly applied law.”<sup>24</sup> In states with complex laws, employer backing has also come from emphasizing that eliminating “routine practices” is not the aim of reforms, as “[e]mployers legitimately contract every day with other independent businesses, typically to perform specialty jobs that the contractor performs for a variety of customers.”<sup>25</sup>

A dramatic boom of legislating activity around misclassification has occurred across the country. Twenty-two states have passed one or more statutes between 2004 and 2012 to alter their prior requirements for designating independent contractors or to alter the enforcement structure or penalties used against employers who fail to do so correctly.<sup>26</sup> Four states, (Washington, Massachusetts, New Mexico, and Oregon), began their new focus on misclassification before the economic recession in 2007.<sup>27</sup> Since then, the wave of statutes has grown every year. In 2007, five

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<sup>20</sup> See Press Release, TJ Donovan Receives Support of Vermont Building and Construction Trades Council, (June 19, 2012), available at <http://vtdigger.org/2012/06/19/tj-donovan-receives-support-of-vermont-building-and-construction-trades-council/>.

<sup>21</sup> See *Fight Against Misclassification Fraud Moves Forward in MN*, N. COUNTRY CARPENTER, May - Aug. 2009, at 4, available at <http://www.northcountrycarpenter.org/magazines/August%202009%20magazine.pdf> (“A series of new laws advocated by our union that regulates independent contractors in the construction industry became Minnesota law January 1, 2009.”).

<sup>22</sup> Bolte, *supra* note 9.

<sup>23</sup> See, e.g., STATE OF CONN. JOINT ENFORCEMENT COMM’N ON EMP. MISCLASSIFICATION, ANNUAL REPORT 2 (2011), <http://www.ctdol.state.ct.us/wgwkstnd/JEC/JEC.pdf> (noting Connecticut increased penalties for misclassification after receiving “substantial feedback from the business community that existing penalties were insufficient”).

<sup>24</sup> Jim Bruson, *Oregon Changes the Definition of “Independent Contractor,”* CONSTRUCTION CONTRACTORS BULL. BOARD, 7 (Oct. 2005), <http://www.oregon.gov/CCB/Documents/pdf/Oct05.pdf>.

<sup>25</sup> *Leveling the Playing Field: Protecting Workers and Businesses Affected by Misclassification: Hearing Before the S. Comm. on Health, Educ., Labor & Pensions*, 111th Cong. 2 (2010) (statement of Catherine K. Ruckelshaus, Legal Co-Director, National Employment Law Project), available at <http://www.help.senate.gov/imo/media/doc/Ruckelshaus.pdf>.

<sup>26</sup> See *supra* note 11.

<sup>27</sup> See An Act Relating to Employment, 1991 Wash. Legis. Serv. ch. 246 (West) (amending WASH. REV. CODE ANN. § 50.04.140 (West 2014)) (effective Jan. 1, 1992); An Act Further Regulating Public Construction in the Commonwealth, 2004 Mass. Legis. Serv. ch. 139 (West) (codified as amended in scattered sections of MASS. GEN. LAWS

states set misclassification legislation into effect;<sup>28</sup> in 2008, two more joined;<sup>29</sup> in 2009, six states passed laws relevant to independent contracting and misclassification;<sup>30</sup> in 2010 eight states legislated on the issue;<sup>31</sup> five additional legislative changes came online in 2011;<sup>32</sup> and 2012 saw

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ANN. (West 2004)) (effective July 19, 2004); Act of April 4, 2005, 2005 N.M. Laws ch. 94, (codified at N.M. STAT. ANN. § 60-13-3.1 (West 2005)) (effective June 17, 2005); An Act Relating to Independent Contractors, 2005 Or. Laws ch. 533 (West) (codified as amended at OR. REV. STAT. ANN. §§ 310.800, 316.162, 670.600, 670.605, 657.040 (West 2006)) (effective Jan. 1, 2006).

<sup>28</sup> See Act of May 25, 2007, 2007 Minn. Sess. Law Serv. ch. 135 (West) (codified as amended in scattered sections of MINN. STAT. ANN. (West 2007)); An Act Concerning Penalties for Concealing Employment or Other Information Related to Workers' Compensation Premiums, 2008 Conn. Legis. Serv. P.A. 07-89 (West) (codified as amended at CONN. GEN. STAT. ANN. §§ 31-288, 31-69a, 31-76a (West 2007)); Construction Industry Independent Contractor Act, 2007 N.J. Sess. Law Serv. ch. 114 (West) (codified at N.J. STAT. ANN. §§ 34:20-1 to 34:20-11 (West 2007)) (effective July 13, 2007); Act of July 17, 2007, 2007 N.H. Adv. Legis. Serv. ch. 362 (LexisNexis) (codified as amended at N.H. REV. STAT. ANN. §§ 275:4, 275:42, 275-E:1, 279:1, 281-A:2, 6:12 (2012)) (effective Jan. 1, 2008); Employee Classification Act, 2007 Ill. Laws 26 Legis. Serv. ch. 26 (West) (codified at 820 ILL. COMP. STAT. ANN. 185/1 to 185/999 (West 2007)) (effective Jan. 1, 2008).

<sup>29</sup> See Act of Mar. 20, 2008, 2008 Wash. Legis. Serv. ch. 102 (West) (codified as amended at WASH. REV. CODE ANN. §§ 50.04.145, 51.08.070, 51.08.180, 51.08.181, 51.08.195 (West 2008)) (effective June 12, 2008); An Act Concerning Employee Misclassification, 2008 Conn. Legis. Serv. P.A. 08-156 (West) (codified at CONN. GEN. STAT. ANN. §§ 31-57h, 31-57i (West 2008)) (effective July 1, 2008).

<sup>30</sup> See An Act Concerning the Misclassification of Employers as Independent Contractors, 2009 Colo. Sess. Laws ch. 406 (codified at COLO. REV. STAT. ANN. § 8-72-114 (2009)) (effective June 2, 2009); Act of July 28, 2009, 2009 Or. Laws ch. 845 (West) (codified at OR. REV. STAT. ANN. §§ 670.700, 670.705 (West 2009)) (effective July 1, 2009); An Act to Ensure that Construction Workers Are Protected by Workers' Compensation Insurance, 2009 Me. Legis. Serv. ch. 452 (West) (codified as amended at ME. REV. STAT. ANN. tit. 26, §§ 1302-A, 1312, tit. 39-A, §§ 102, 105-A (2009)) (effective Sept. 12, 2009); Workplace Fraud Act of 2009, 2009 Md. Code Ann. Adv. Legis. Serv. ch. 188 (LexisNexis) (codified as amended in scattered sections of MD. CODE ANN., LAB. & EMPL. (LexisNexis 2009)) (effective Oct. 1, 2009); Workplace Fraud Act, 77 Del. Laws ch. 192 (2009) (codified at DEL. CODE ANN. tit. 19, §§ 3501-3514 (West 2009)) (effective Oct. 29, 2009); An Act to Amend the Indiana Code Concerning Labor and Safety, 2009 Ind. Legis. Serv. ch. 164 (West) (codified at IND. CODE ANN. §§ 6-8.1-3-21.2, 22-1-1-22, 22-3-1-5, 22-4.1-4-4 (West 2010)) (effective Jan. 1, 2010).

<sup>31</sup> See Act of March 25, 2010, 2010 Ind. Legis. Serv. P.L. 110-2010 (West) (codified as amended in scattered sections of IND. CODE ANN. (West 2010)) (effective July 1, 2010); An Act Relating to Misclassification of Employees to Lower Premiums for Workers' Compensation and Unemployment Compensation, 2010 Vt. Legis. Serv. ch. 142 (West) (codified as amended in scattered sections of VT. STAT. ANN. (West 2010)) (effective July 1, 2010); An Act To Amend the Laws Governing the Misclassification of Construction Workers, 2010 Me. Legis. Serv. ch. 649 (West) (codified as amended at ME. REV. STAT. ANN. tit. 39-A, § 105-A (2010)) (effective July 12, 2010); Employee Classification Act, 2010 Neb. Laws ch. 563 (codified at NEB. REV. STAT. ANN. §§ 48-2901 to 48-2912 (LexisNexis 2010)) (effective July 15, 2010); An Act Implementing the Recommendations of the Joint Enforcement Commission on Employee Misclassification, 2010 Conn. Legis. Serv. P.A. 10-12 (West) (codified as amended at CONN. GEN. STAT. ANN. §§ 31-69a, 31-288 (West 2010)) (effective Oct. 10, 2010); New York State Construction Industry Fair Play Act, 2010 N.Y. Sess. Laws ch. 418 (McKinney) (codified at N.Y. LAB. LAW §§ 861 to 861-f (McKinney 2010)) (effective Oct. 26, 2010); Act of May 12, 2010 2009 Wis. Legis. Serv. ch. 292 (West) (codified at WIS. STAT. ANN. §§ 103.005(10), 103.06 (West 2011)) (effective Jan. 1, 2011); Construction Workplace Misclassification Act, 2010 Pa. Legis. Serv. ch. 72 (West) (codified at 43 PA. STAT. ANN. §§ 933.1-933.17 (West 2011)) (effective Feb. 10, 2011).

<sup>32</sup> See Worker Classification Coordinated Enforcement Act, 2011 Utah Laws ch. 15 (codified at UTAH CODE ANN. §§ 34-47-101 to 34-47-202 (LexisNexis 2011)) (effective Mar. 7, 2011); Construction Licensees Related Amendments, 2011 Utah Laws ch. 413 (codified as amended in scattered sections of UTAH CODE ANN. (LexisNexis 2011)) (effective July 1, 2011); Act of May 12, 2011, 2011 Kan. Sess. Laws ch. 81 (codified as amended at KAN. STAT. ANN. §§ 44-703, 44-766, 79-3234 (West 2011)) (effective July 1, 2011); An Act Concerning Independent Contractors in

three states take legislative action.<sup>33</sup>

This Article seeks to provide an analysis of this quickly changing legal landscape by closely examining the array of new statutes as well as the case law applying them. While previous articles have discussed widespread misclassification, few articles have examined the effectiveness of the legislative solutions currently being implemented. Recent scholarship has largely focused on critiquing the traditional common law independent contractor analysis and on suggesting improvements.<sup>34</sup> That traditional test uses many non-dispositive factors to assess the control an employer has over a worker.<sup>35</sup> It has been criticized for being easily manipulated by employers and for generating uncertainty over a worker's employee status.<sup>36</sup> Scholars have also focused on legislative adaptations to the independent contractor test, proposing reformulations of the test, or alternative legislative solutions to increase liability for misclassification.<sup>37</sup> Other scholars have suggested innovative common law causes of action to protect workers against misclassification, and to allow them to obtain redress when misclassification occurs.<sup>38</sup>

A handful of articles have discussed the recent wave of legislation modifying the independent contractor definition or penalties for misclassification, but they have either only provided a preliminary description of the different statutory models,<sup>39</sup> or focused solely on a particular subset of statutes.<sup>40</sup> This Article expands on these analyses, providing an inventory of

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the Trucking and Messenger Courier Industries, 2011 Me. Legis. Serv. ch. 176 (West) (codified at ME. REV. STAT. ANN. tit. 39-A § 114 (2011)) *repealed by* An Act to Standardize the Definition of "Independent Contractor," 2012 Me. Legis. ch. 643 (West 2012); Act of Oct. 9, 2011, 2011 Cal. Legis. Serv. ch. 706 (West) (codified at CAL. LAB. CODE §§ 226.8, 2753 (West 2012)) (effective Jan. 1, 2012).

<sup>33</sup> See Act of May 2, 2012, 2012 Md. Code Ann. Adv. Legis. Serv. ch. 206 (LexisNexis) (codified as amended at MD. CODE ANN., LAB. & EMPL. §§ 3-903, 3-903.1, 3-905, 3-906, 3-913 (LexisNexis 2012)) (effective July 1, 2012); Act of May 31, 2012, 2012 Kan. Sess. Laws ch. 166 (West) (codified as amended in scattered sections of KAN. STAT. ANN. (West 2012)) (effective July 1, 2012); An Act to Standardize the Definition of "Independent Contractor," 2012 Me. Legis. ch. 643 (West) (codified at ME. REV. STAT. ANN. tit. 1, § 1012, tit. 5, § 19, tit. 26, §§ 591, 591-A, 1043, tit. 39-A, §§ 102, 105-A, 401 (West 2012)) (effective Dec. 31, 2012).

<sup>34</sup> See Stephen F. Befort, *Labor and Employment Law at the Millennium: A Historical Review and Critical Assessment*, 43 B.C. L. REV. 351, 418-21 (2002) (critiquing the common law test); See generally Richard R. Carlson, *Why the Law Still Can't Tell an Employee When It Sees One and How It Ought to Stop Trying*, 22 BERKELEY J. EMP. & LAB. L. 295, 306-52 (2001) (providing a comprehensive analysis of the development of the common law control test, economic realities test, and exploring the problems with both tests).

<sup>35</sup> See Carlson, *supra* note 34, at 298-99.

<sup>36</sup> Befort, *supra* note 34, at 418-21; Carlson, *supra* note 34, at 335-36.

<sup>37</sup> Carlson, *supra* note 34, at 301 (proposing a test that focuses on transactions between parties, rather than employee status); Karen R. Harned et al., *Creating a Workable Legal Standard for Defining an Independent Contractor*, 4 J. BUS. ENTREPRENEURSHIP & L. 93, 95, 113 (2010) (arguing for a one factor legal "step back" test, that would reduce uncertainty for businesses and the government); Jenna Amato Moran, *Independent Contractor or Employee? Misclassification of Workers and Its Effect on the State*, 28 BUFF. PUB. INT. L.J. 105, 129-30 (2010) (suggesting a third category of workers, "dependent contractors," who would enjoy some of the same benefits as employees).

<sup>38</sup> See, e.g., Jean Tom, Note, *Is A Newscarrrier an Employee or an Independent Contractor? Deterring Abuse of the "Independent Contractor" Label Via State Tort Claims*, 19 YALE L. & POL'Y REV. 489, 501-02 (2001) (proposing that the use of state tort claims of fraudulent and negligent misrepresentation could be a powerful tool to hold employers liable for misclassification of employees).

<sup>39</sup> See, e.g., Jason M. Goldstein, *Money under the Bridge: The Worker Misclassification Problem*, 5 FLA. A & M U. L. REV. 107, 125-29 (2009) (providing a brief overview of state legislation addressing independent contractor misclassification).

<sup>40</sup> See, e.g., Christopher Buscaglia, *Crafting a Legislative Solution to the Economic Harm of Employee*

misclassification legislation recently passed or amended in twenty-two states, including statutes passed since previous articles were written. In Part I of this Article, we appraise the federal context during which this state legislative action has occurred. In Part II, we provide a statutory analysis of recent misclassification legislation, including an investigation of the most effective features and the apparent weaknesses. Our analysis evaluates, in greater detail than prior articles, specific statutory features and language, considering both alterations to independent contractor definitions and strengthened penalties for misclassification.

In Part III, this Article provides an analysis of how these statutes have fared in practice, through an analysis of case law under the new statutes, an additional step beyond previous scholarly work that has focused on statutory language. In particular, we focus on limitations that still exist under current statutory schemes, as well as common arguments employers have made to avoid liability. Throughout our analysis of employer and court responses, we also suggest ways to strengthen statutes and to use common law arguments to prevent the current statutory weaknesses from being exploited by employers.

We believe that objective and predictable definitions benefit most workers. Prior complex legal regimes have made compliance challenging for even well-intentioned businesses, beyond employers deliberately taking advantage of weak or unenforced misclassification laws or those succumbing to the economic pressure of widespread industry practices.<sup>41</sup> Our comparison of the variety of statutory models underscores that efficacy will likely vary, including by the clarity of reformed laws and the strength of incentives provided by the new laws. Future legislative efforts should replicate penalty statutes and the codification of a presumption of employee status with a simplified exception for independent contractors, frequently called the “ABC” test.

Early adjudications under the new statutes also show that some employers are seeking alternative business models or are finding new strategies to avoid liability for misclassifying their workers. Distinct from prior employer practices, these tactics—such as companies simply disappearing or crafting creative legal arguments to dodge accountability—may allow employers to find safe havens where they are more fully insulated from the reach of the law. Employee plaintiffs may be best served not only by strengthening statutes to close off these loopholes, but also by using common law arguments to prevent employers from successfully exploiting such loopholes.

## I. FEDERAL CONTEXT AND COORDINATION WITH STATES’ MISCLASSIFICATION CRACKDOWNS

A worker’s status, as an independent contractor or employee, determines his eligibility for federal payroll taxes as well as for Social Security, Medicare, and federal worker protections, such as those under the Fair Labor Standards Act.<sup>42</sup> While states currently appear to have taken the lead in fighting employee misclassification, national attention on misclassification has grown as concerns have mounted over both losses to federal tax collection and employers escaping the

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*Misclassification*, 9 U.C. DAVIS BUS. L.J. 111, 120-26 (2009) (analyzing in detail five recent statutes that directly penalize for misclassification and discussing the consequences for states without such statutes).

<sup>41</sup> See Mark Wiletsky, *Worker Misclassification Poses Serious Risks for Businesses*, COLORADOBIZ MAGAZINE, Dec. 2010.

<sup>42</sup> See Hintze, *supra* note 2.

reach of federal regulatory worker protections.<sup>43</sup> Relative to the entire national workforce, the scale of independent contracting is not vast: in 2005, the Bureau of Labor Statistics reported there were 10.3 million independent contractors nationally, comprising 7.4% percent of the workforce.<sup>44</sup> Nonetheless, according to Congressman Richard Neal, the Government Accountability Office estimates that worker misclassification costs the federal treasury \$4.7 billion annually in income tax revenues.<sup>45</sup>

Simultaneous to local misclassification legislating and enforcement, federal enforcement has expanded, led primarily by the Department of Labor (DOL) and the Internal Revenue Service (IRS). In 2007, the IRS delivered a bill to FedEx for \$319 million in back taxes and interest, asserting that a 2002 audit indicated the company had misclassified its more than 13,000 drivers as independent contractors.<sup>46</sup> While FedEx initially won a reversal,<sup>47</sup> the Ninth Circuit recently held that a class of FedEx drivers were employees and had been misclassified as independent contractors.<sup>48</sup> More influential than any ultimate tab to the federal government, the FedEx case successfully signaled the IRS's seriousness about identifying employee misclassification and enforcing compliance. Recent years have seen similar efforts by the DOL's Wage and Hour Division: in 2010, the agency collected almost four million dollars in back wages for minimum wage and overtime violations from misclassification investigations, an almost four hundred percent increase over the \$1.3 million the division collected in 2008.<sup>49</sup> In 2010, President Obama's federal budget anticipated the inclusion of "at least \$7 billion over 10 years," yielded from misclassification crackdowns by various agencies.<sup>50</sup>

The IRS has also steered the national response to misclassification away from punishments for violations and towards incentives for compliance. In September 2011, it announced the Voluntary Classification Settlement Program, which encourages employers to voluntarily reclassify as employees workers whom they have treated as independent contractors for three years.<sup>51</sup> The employers cannot escape all federal payroll tax liability, but "can obtain substantial relief" via a reduced obligation of about one percent of a year's wages for the

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<sup>43</sup> Steven Greenhouse, *U.S. Cracks Down on 'Contractors' as a Tax Dodge*, N.Y. TIMES (Feb. 18, 2010), <http://www.nytimes.com/2010/02/18/business/18workers.html>.

<sup>44</sup> Economic News Release, U.S. Dep't of Labor, Bureau of Labor Statistics, *Contingent and Alternative Employment Arrangements, February 2005*, BUREAU OF LABOR STATISTICS, (July 27, 2005), <http://www.bls.gov/news.release/conemp.nr0.htm>.

<sup>45</sup> *Effects of Misclassifying Workers as Independent Contractors: Hearing Before the H. Subcomm. on Income Sec. & Family Support and Subcomm. on Select Revenue Measures of the Comm. on Ways & Means*, 110th Cong. (2007) (statement of Richard E. Neal, Chairman, H. Subcomm. on Select Revenue Measures).

<sup>46</sup> Todd D. Saveland, *FedEx's New "Employees": Their Disgruntled Independent Contractors*, 36 TRANSP. L.J. 95, 115 (2009).

<sup>47</sup> Wayne Risher, *IRS Reverses Assessment over Status of FedEx Drivers*, Com. Appeal (Oct. 23, 2008, 9:49 AM), <http://www.commercialappeal.com/business/government-bolsters-fedex-claims-about-its-drivers>.

<sup>48</sup> See *Alexander v. FedEx Ground Package Sys.*, 765 F.3d 981, 997 (9th Cir. 2014).

<sup>49</sup> See Joshua Kirkpatrick & Stephanie Hankin, *Colorado Latest to Join U.S. DOL to Reduce Worker Misclassification*, LITTLER (Dec. 14, 2011), <http://www.littler.com/publication-press/publication/colorado-latest-join-us-dol-reduce-worker-misclassification>.

<sup>50</sup> Greenhouse, *supra* note 43.

<sup>51</sup> *IRS Announces New Voluntary Worker Classification Settlement Program; Past Payroll Tax Relief Provided to Employers Who Reclassify Their Workers*, IRS (Sept. 21, 2011), <http://www.irs.gov/uac/IRS-Announces-New-Voluntary-Worker-Classification-Settlement-Program%3B-Past-Payroll-Tax-Relief-Provided-to-Employers-Who-Reclassify-Their-Workers>.

reclassified workers, without any interest or penalties.<sup>52</sup> The program focuses on the need to “provide certainty and relief to employers” by allowing them to resolve classification issues “at a low cost” to “give [employers] a fresh start with their tax obligations.”<sup>53</sup> However, this incentive may be diminished, as the IRS cannot offer to wipe away back payments, penalties, or interest to other federal or state agencies, a weakness emphasized by the program’s critics.<sup>54</sup>

To fortify and streamline federal investigations, in September 2011 the IRS and DOL signed a Memorandum of Understanding (MOU) to enable information sharing and coordination, citing the need to “level the playing field for law-abiding employers and ensure that employees receive the protections to which they are entitled.”<sup>55</sup> The DOL’s Wage and Hour Division has also signed similar MOUs to facilitate information sharing with their counterpart agencies in more than a dozen states.<sup>56</sup> Arguably, these agreements not only improve federal investigatory efforts but also provide a multiplier effect for the consequences of state enforcements, which can now directly lead to federal tax liabilities, enlarging the incentives against misclassification.

Still, federal activity remains entirely limited to these enforcement tactics, though multiple bills related to misclassification have been introduced in Congress. As a senator, President Obama advocated for federal legislation on the topic.<sup>57</sup> President Obama’s White House has expressed support for at least three bills,<sup>58</sup> perhaps indicating an opportunity for passage given recent focus on federal deficits and on closing tax loopholes. While all three proposals include increased misclassification penalties, their forms otherwise vary. The Taxpayer Responsibility, Accountability, and Consistency Act of 2009 would empower independent contractors to petition the IRS for a determination about their status, while also shifting the burden to employers to demonstrate their reasonable basis for classifying workers as independent contractors.<sup>59</sup> Provisions of the Fair Playing Field Act, introduced in both 2010 and 2012, include removing the legal safe harbor against IRS prosecution of employers who consistently treat workers as independent contractors and provide a reasonable basis for doing so to the IRS.<sup>60</sup> The act would

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<sup>52</sup> *Id.* Other program requirements include an application sixty days before the desired reclassification date. *Id.* While employers will not be audited on payroll taxes for prior years related to such workers, any employer already being audited by the IRS, DOL, or a state agency pertaining to worker classification is ineligible. *Id.*

<sup>53</sup> *Id.* (quoting IRS Commissioner Doug Shulman).

<sup>54</sup> John Browning, *The IRS Gets Tough on Employers*, D CEO MAGAZINE, May-June, 2012, available at <http://www.dmagazine.com/publications/d-ceo/2012/may-june/the-irs-gets-tough-on-employers>.

<sup>55</sup> News Release, *Labor Secretary, IRS Commissioner Sign Memorandum of Understanding to Improve Agencies’ Coordination on Employee Misclassification Compliance and Education*, DEP’T OF LABOR (Sept. 19, 2011), <http://www.dol.gov/opa/media/press/whd/WHD20111373.htm>.

<sup>56</sup> See *Misclassification of Employees as Independent Contractors*, Dep’t of Labor, <http://www.dol.gov/whd/workers/misclassification/stateinfo-nojs.htm> (last visited Jan. 22, 2015). The states whose agencies have signed MOUs are: California, Colorado, Connecticut, Hawaii, Illinois, Iowa, Louisiana, Maryland, Massachusetts, Minnesota, Missouri, Montana, Utah, and Washington. *Id.*

<sup>57</sup> See Robert Wood, *White House on Contractor vs. Employee: There Will Be Blood*, FORBES, (Sept. 17, 2010, 7:00AM), <http://www.forbes.com/sites/robertwood/2010/09/17/white-house-on-contractor-vs-employee-there-will-be-blood/>.

<sup>58</sup> See *id.*

<sup>59</sup> *Bill Would Clarify Independent Contractor Rules*, LITTLER (Aug. 4, 2009), <http://www.littler.com/dc-employment-law-update/bill-would-clarify-independent-contractor-rules-increase-employer-penalties>.

<sup>60</sup> *Fair Playing Field Act of 2012: Congress Trying Again to End ‘Safe Harbor’ for Businesses that May Have Misclassified Employees as Independent Contractors*, PEPPER HAMILTON (March 5, 2012), [http://www.pepperlaw.com/publications\\_update.aspx?articlekey=2314](http://www.pepperlaw.com/publications_update.aspx?articlekey=2314).

also create a “Miranda warning for independent contractors,” by requiring written disclosure about federal tax obligations and the provision of information about employment and labor issues.<sup>61</sup> Finally, the 2011 Employee Misclassification Prevention Act would amend the Fair Labor Standards Act to demand direct notice to workers about their classification status and right to challenge that classification, and impose recordkeeping requirements.<sup>62</sup>

## II. ANALYSIS OF RECENT STATE INDEPENDENT CONTRACTING LEGISLATION

Legislative action limiting the use of and penalizing the abuse of independent contractor status for workers has been as varied as states themselves. Each state has tailored its strategy to the distinct state statutory baseline governing local independent contracting. Some states have chosen to directly modify the legal requirements for a business to validly use independent contractors. Such a redefinition strategy has taken multiple forms. In some instances, states have revised the definitions of independent contracting relevant to singular employee benefits, such as workers compensation or unemployment insurance, either to bring that definition in line with others or to test a more rigorous standard. Other states have more ambitiously transformed their misclassification status quo by setting a universally applicable independent contracting standard across agencies and employer obligations.

Some states have instead increased enforcement of existing laws, through amplified investigative efforts, or strengthened penalties for businesses caught misclassifying employees. Multiple states have accomplished this strategy without direct legislative change, via the use of task forces that coordinate enforcement resources and information across various state agencies. In a subset of states focused on increasing compliance through stronger penalties, statutes have altered liability standards, including the introduction of criminal penalties for misclassification. Definitional and enforcement strategies have been implemented both independently and in tandem.

In addition, a group of states has enacted legislation targeting a single industry, almost solely the local construction industry, seen as the hub of the most egregious and pervasive misclassification practices. These statutes have tended to be more comprehensive than the universally applicable statutes and have often combined altered definitions with increased penalties and enforcement strategies.

### A. “Definitional” Statutes

Sixteen states—a majority of those that have recently addressed misclassification through legislation—have altered their statutory definitions of independent contracting or employment relationships.<sup>63</sup> In many ways, these definitions are at the heart of the matter.

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<sup>61</sup> Wood, *supra* note 57.

<sup>62</sup> See Kirkpatrick & Hankin, *supra* note 49.

<sup>63</sup> DEL. CODE ANN. tit. 19, § 3501 (West 2014); 820 ILL. COMP. STAT. ANN. 185/10; (West 2014); KAN. STAT. ANN. § 44-703 (West 2014); ME. REV. STAT. ANN. tit. 39-A, § 102(13-A) (2014); MD. CODE ANN., LAB. & EMPL. § 3-903 (LexisNexis 2014); MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014); MINN. STAT. ANN. § 181.723 (West 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014) (referencing NEB. REV. STAT. ANN. § 48-604(5)(a) (LexisNexis 2014)); N.H. REV. STAT. ANN. § 275:4 (2014); N.J. STAT. ANN. § 34:20-4 (West 2014); N.M. STAT. ANN. § 60-13-3.1 (West 2014); N.Y. LAB. LAW § 861-c (McKinney 2014); OR. REV. STAT. ANN. § 670.600 (West 2014); 43 PA. STAT. ANN. § 933.3 (West 2014); UTAH CODE ANN. § 34A-2-103 (LexisNexis 2014); WASH. REV. CODE ANN. § 50.04.140 (West 2014).

Without clear communication of which workers are and are not independent contractors, businesses struggle to comply with the law when attempting to legitimately use independent contractors, workers are less likely to be aware of misclassification or to pursue a remedy, and state agencies must expend resources to implement increased penalties and strengthen enforcement mechanisms.<sup>64</sup> All of these complications enable businesses to succeed at deliberately misclassifying workers.

States have variously simplified their independent contractor definitions, refocused on new indicia of independence, and standardized definitions across a variety of relevant benefits and employer obligations. Across the nation, many states include contrasting definitions within distinct areas of their statutory systems, such as those governing claims and benefits, taxes, unemployment insurance, or workers compensation. Thus, legislatively shifting the definition of an independent contractor to prevent misclassification requires more than merely identifying the clearest or fairest test. Instead, it is a matter of unifying and simplifying the standard: both the test itself and its consistent application across relevant laws.

### 1. The Three-Prong ABC Test and Its Reach

In 2004, Massachusetts made its most recent alteration to its statutory definition of independent contracting, a simplified version of the common law “right to control” factors with a presumption of employment surmountable only by satisfying a three-prong assessment commonly referred to as the “ABC” test. The three factors as laid out in the Massachusetts and other state statutes are: (A) that “the individual is free from direction and control,” applicable both “under his contract for the performance of service and in fact,” (B) that “the service is performed outside the usual course of business of the employer,” and (C) that the “individual is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service performed.”<sup>65</sup> Massachusetts did not create the ABC test,<sup>66</sup> but, as discussed in depth below, the ABC formulation and variations on it has come to dominate reform of independent contracting definition laws in other states.<sup>67</sup> It is of note that this Part examines only recent statutory changes; other states already have ABC tests and similar definitional constructions in all or some of their relevant statutes, but an analysis of the full use of the ABC test across the country is outside the scope of this Article.

In contrast to the ABC formulation, many states’ common law, the IRS, and some state statutes use tests that identify a legitimate independent contractor by functionally analyzing the ability of the employer (or “payer”) to “control or direct only the result of the work and not what will be done and how it will be done.”<sup>68</sup> Despite this shared theme, independent contracting definitions have instead traditionally provided factors for consideration.

Since 1987, the IRS has considered twenty or more factors, to identify the existence of

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<sup>64</sup> See Wiletsky, *supra* note 41.

<sup>65</sup> MASS. GEN. LAWS ANN. ch. 149, § 148B(a)(1)-(3) (West 2014).

<sup>66</sup> See, e.g., R. Stell, *Independent Contractors and ABC Test Reform in Maine*, NAT’L FED’N OF INDEP. BUS. (Mar. 31, 2006), <http://www.nfib.com/nfib-in-my-state/nfib-in-my-state-content?cmsid=27943> (indicating that Maine adopted the ABC test in 1935).

<sup>67</sup> See, e.g., R. Stell, *Independent Contractors and ABC Test Reform in Maine*, NAT’L FED’N OF INDEP. BUS. (Mar. 31, 2006), <http://www.nfib.com/nfib-in-my-state/nfib-in-my-state-content?cmsid=27943>.

<sup>68</sup> *Independent Contractor Defined*, IRS (last updated Oct. 2, 2014), <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Independent-Contractor-Defined>.

an employer-employee relationship; the list was derived from the common law “right to control” tests and so provides a helpful summary.<sup>69</sup> The factors are organized into three categories: “behavioral control,” “financial control,” and “type of relationship,” and no factor is given specific weight or treated as dispositive.<sup>70</sup> The behavioral control categories are: (1) instruction type, (2) degree of instruction, (3) evaluation systems and (4) training of the worker.<sup>71</sup> To evaluate financial control, the IRS considers the ability of the business to “control the economic aspects of worker’s job,” considering: (5) significant investment, (6) unreimbursed expenses, (7) opportunity for profit or loss, (8) services available to the market or other businesses, and (9) the method of payment.<sup>72</sup> Finally, in considering how the parties themselves “perceive their relationship to each other,” the IRS examines the presence or absence of (10) written contracts, (11) employee benefits, (12) permanency of the relationship, and (13) “[s]ervices provided as key activity of the business.”<sup>73</sup> Common law “right to control” tests implement similar non-dispositive factors regarding the control or direction of the means of work.<sup>74</sup>

In the eight years from 2004 to 2012, sixteen states—including Maine twice, once regarding its trucking and courier industries<sup>75</sup> and once regarding its unemployment compensation statute<sup>76</sup>—have transformed the legal requirements to be an independent contractor.<sup>77</sup> All of these states except two have implemented ABC tests or related formulations. Specifically, Kansas and Maine chose definitions that use sets of factors resembling common law control tests.<sup>78</sup> Some of

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<sup>69</sup> JOINT COMM. ON TAXATION, PRESENT LAW AND BACKGROUND RELATING TO WORKER CLASSIFICATION FOR FEDERAL TAX PURPOSES, JCX-26-07 2-5 (2007) available at <http://www.irs.gov/pub/irs-utl/x-26-07.pdf>.

<sup>70</sup> See *Topic 762—Independent Contractor vs. Employee*, IRS, <http://www.irs.gov/taxtopics/tc762.html> (last updated July 16, 2014); JOINT COMM. ON TAXATION, *supra* note 69 at 5.

<sup>71</sup> *Behavioral Control*, IRS, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Behavioral-Control> (last updated July 14, 2014).

<sup>72</sup> *Financial Control*, IRS, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Financial-Control> (last updated July 14, 2014).

<sup>73</sup> *Type of Relationship*, IRS, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Type-of-Relationship> (last updated Aug. 28, 2014).

<sup>74</sup> See *Topic 762—Independent Contractor vs. Employee*, *supra* note 70. Common law “right to control” tests include factors such as: the nature and degree of control or instruction, whether a distinction exists between business or occupation of a worker and an employee, whether work is done with supervision, the amount of skill required, the amount of tools or materials the worker provides and if work site is provided by employer, the permanency of the relationship, the method of payment (based on time or by project), the extent to which the services rendered are integral or needed or part of regular business, the intent of involved parties as to the character of the relationship; and whether the worker may be employed by more than one firm or employer. See *Independent Contractor (Self-Employed or Employee?)*, IRS (last updated Oct. 2, 2014) <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Independent-Contractor-Self-Employed-or-Employee>.

<sup>75</sup> An Act Concerning Independent Contractors in the Trucking and Messenger Courier Industries, 2011 Me. Legis. Serv. ch. 176 (West) (codified at ME. REV. STAT. ANN. tit. 39-A, § 114 (2011)), *repealed by* An Act to Standardize the Definition of “Independent Contractor,” 2012 Me. Legis. ch. 643 (West 2012).

<sup>76</sup> An Act to Standardize the Definition of “Independent Contractor,” 2012 Me. Legis. ch. 643 (West) (codified at ME. REV. STAT. ANN. tit. 1, § 1012, tit. 5, § 19, tit. 26, §§ 591, 591-A, 1043, tit. 39-A, §§ 102, 105-A, 401 (West 2012)) (effective Dec. 31, 2012).

<sup>77</sup> See *supra* note 63.

<sup>78</sup> See KAN. STAT. ANN. § 44-703(i)(3)(D) (West 2014) (codifying a “right to control” test); ME. REV. STAT. ANN. tit. 39-A, § 102(13-A) (2014) (codifying a presumption of employee status with several required factors to overcome that status); ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014) (codifying a free from control factor test with

these changes apply to only a portion of the state's statutory scheme, either specific benefits or certain industries or workers, as will be discussed in further detail below. The ABC test, coupled with a presumption of employee status unless the employer demonstrates compliance, has been the clearly favored test of state legislatures; most of these states adopted a clear or recognizable ABC formulation.<sup>79</sup> In contrast, some states have made notable variations in the phrasing of the ABC test. For example, three states, Pennsylvania, New Mexico, and Oregon, established a hybrid definition, replacing the "B" or "usual course of business" prong with either additional factors or requirements to satisfy "C," "customarily engaging in an independently established trade."<sup>80</sup> And, irrespective of the use of ABC or another formulation, all sixteen states' statutes, except for Kansas's and Maine's unemployment compensation statutes, either explicitly or implicitly made employee status the presumption by utilizing a list of mandatory criteria rather than a set of subjectively weighted factors.<sup>81</sup>

## 2. Variations on the ABC Language and Structure

Despite the domination of the ABC formulation, states have made small and large modifications to the language of each prong, which merit closer analysis to identify disadvantages and worthy improvements. Worker advocates have called ABC the "most objective" test and "the most difficult for employers to manipulate."<sup>82</sup> Still, one academic, Professor Buscaglia,

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five mandatory factors and seven additional criteria, three of which must be satisfied).

<sup>79</sup> See, e.g., DEL. CODE ANN. tit. 19, §§ 3501(a)(7), 3503(c) (West 2014) (using the ABC formula without alteration with an implicit presumption); MD. CODE ANN., LAB. & EMPL. § 3-903(c)(1) (LexisNexis 2014) (using altered ABC factors, such as showing the freedom from direction and control both under contract and in fact, with an explicit presumption of employee status).

<sup>80</sup> N.M. STAT. ANN. § 60-13-3.1(A) (West 2014) (establishing additional factors including that "the person providing labor or services is responsible for obtaining business registrations or licenses required by state law[,] . . . furnishes the tools or equipment necessary to provide the labor or services[,] . . . has the authority to hire and fire employees to perform the labor or services," and that payment "is made upon completion of the performance of specific portions of a project or is made on the basis of a periodic retainer," and listing circumstances that must be met to satisfy what is commonly known as the C prong, that a worker is engaged in an independently established business.); 43 PA. STAT. ANN. § 933.3 (West 2014) (requiring a written contract; in place of the "C" prong to show independently established trade, six factors are required: possesses tools; ability to realize profit or suffer losses from services; proprietary interest in a business; maintenance of separate business location; previously performed or held out as available to perform similar services; maintains liability insurance); OR. REV. STAT. ANN. § 670.600(3)(a-e) (West 2014) (lacking a "B" prong; its "C" prong mandates three of five factors to show an independently established trade: a separate location; bearing risk of loss; at least two clients that year, or an attempt to obtain such clients; a significant investment; and the authority to hire and fire).

<sup>81</sup> ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014) (including a list of optional criteria); KAN. STAT. ANN. § 44-703(i)(3)(D) (West 2014) (specifying a right to control test). Statutes with explicit presumptions include: 820 ILL. COMP. STAT. ANN. 185/10; (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-903 (LexisNexis 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014); N.H. REV. STAT. ANN. § 275:4 (2014); N.J. STAT. ANN. § 34:20-4 (West 2014); N.M. STAT. ANN. § 60-13-3.1 (West 2014); N.Y. LAB. LAW § 861-c (McKinney 2014); 43 PA. STAT. ANN. § 933.3 (West 2014); WASH. REV. CODE ANN. § 50.04.100 (West 2014). Statutes with implicit presumptions from mandatory criteria include: DEL. CODE ANN. tit. 19, § 3501 (West 2014); MINN. STAT. ANN. § 181.723 (West 2014); OR. REV. STAT. ANN. § 670.600 (West 2014); UTAH CODE ANN. § 34A-2-103 (LexisNexis 2014).

<sup>82</sup> CATHERINE K. RUCKELSHAUS & SARAH LEBERSTEIN, NELP SUMMARY OF INDEPENDENT CONTRACTOR REFORMS 5 (2011), available at <http://www.nelp.org/page/-/Justice/2011/2011IndependentContractorReformUpdate.pdf>.

complained that the ABC factors are only deceptively simple and in application are “neither clearer nor easier” than the common law right to control factors that they typically replace.<sup>83</sup> He argued that in application, the prongs’ broad language requires analysis too similar to common law tests; in particular, he focused on the “A” prong and claimed it incorporates common law right to control analysis by requiring courts to “weigh several factors to determine if the employer exercises sufficient control over the work.”<sup>84</sup>

The “A” prong does focus—similarly to the common law test—on the relationship between the parties and the presence of control. Yet, while common law tests may look beyond the language of the contract or may require courts to consider the practical relationship when a contract is absent, Massachusetts’s statute explicitly mandates that freedom from direction and control be demonstrated contractually and in fact,<sup>85</sup> thus amplifying the prong’s demand with a patently objective, although perhaps malleable, requirement. Four other states, Washington, New York, Nebraska, and Maryland, have adopted the “A” prong with the language that requires proof of both contractual language and the employment relationship in fact.<sup>86</sup> In New York, this mechanism’s power has become apparent in decisions by the state’s Workers’ Compensation Board under the new law. In one decision, the absence of a contract trumped evidence that a subcontractor acted free from the control of the prime contractor, by paying its worker who also knew nothing of the prime contractor.<sup>87</sup> Similarly, in another decision regarding a subcontractor without a written contract with its prime contractor, the board indicated the subcontractor’s payment responsibilities and actions as a foreman over other workers were simply undertaken “in addition to” other tasks and “did not endow the claimant with the independent authority” to overcome an absent written contract.<sup>88</sup>

Every other state newly utilizing the “A” factor, whether within a full ABC framework or incorporated into a broader test, has left it to employers, employees, and ultimately to the discretion of courts to assess the absence or presence of freedom from control.<sup>89</sup> Even where the contractual demand is present, these statutes provide no guidance for interpreting a lack of control in fact. As with common law tests, along with the presence of a proper written agreement for independent contracting, the “A” factor still requires evidence that, in practice, the employer has not exerted control. Nebraska’s statute is unique in asserting that all its ABC factors are not intended to be interpreted through common law formulations and “shall be considered completed as written,”<sup>90</sup> perhaps attempting to prevent its statutory reform from being rendered irrelevant by the continued use of common law standards. In contrast, this emphasis on the role of contractual

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<sup>83</sup> Buscaglia, *supra* note 40, at 129. Professor Buscaglia refers to the ABC test as the “3-prong test.” *See id.* at 124, 129.

<sup>84</sup> *Id.* at 129.

<sup>85</sup> MASS. GEN. LAWS ANN. ch. 149, § 148B(a)(1) (West 2014).

<sup>86</sup> *See* WASH. REV. CODE ANN. §§ 50.04.140(1)(a), 50.04.145(1), 51.08.181(1), 51.08.195(1) (West 2014); N.Y. LAB. LAW § 861-c(1)(a) to (c) (McKinney 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014) (referencing NEB. REV. STAT. ANN. § 48-604(5)(a) (LexisNexis 2014)); MD. CODE ANN., LAB. & EMPL. § 3-903 (Lexis 2014).

<sup>87</sup> *Rustuccia Drywall Inc.*, No. 3060 9427, 2011 WL 2661233, at \*1, \*3 (N.Y. Workers’ Comp. Bd. June 29, 2011).

<sup>88</sup> *William A[.] Teague Restorations*, No. G000 4014, 2012 WL 106363, at \*6 (N.Y. Workers’ Comp. Bd. Jan. 6 2012) While *stare decisis* prevented the Board from applying New York’s statutory test, the common law test reached the same result. *See id.* at \*4-6.

<sup>89</sup> *See, e.g.*, DEL. CODE ANN. tit. 19, § 3501 (West 2014).

<sup>90</sup> NEB. REV. STAT. ANN. § 48-604(5) (LexisNexis 2014).

language may provide employers with an opening to contractually designate a worker as an independent contractor, while in reality preserving employee-like control. Still, while the ABC factors may simplify and clarify the process of drawing lines between independent contracting and employment, even they cannot remove the complexity inherent in business and labor structures nor the inevitability of courts applying the tests and reaching differing conclusions under the same facts.

Two of the four states' statutes, New York's and Maryland's, that include the contractual requirement language in the "A" prong apply solely to the construction or landscape industry,<sup>91</sup> indicating that such a high bar may be either appropriate or politically feasible only when regulating an industry known for informal and illegal contracting structures. Moreover, the distinct attention arising from a singular industry being the subject of a legislative change arguably places its employers and workers on notice of new demands, including the need for a written contract to validly work outside employee status.

Notably, three other states with legislation targeted at the construction industry have eliminated the "B" (course of business) prong and instead incorporated a requirement for a written contract or a license, parallel to the "A" contractual requirement in formalizing a legitimate independent contractor: Pennsylvania's construction-only statute explicitly demands a written contract;<sup>92</sup> New Mexico's construction law includes licensure as an added factor;<sup>93</sup> and Oregon's universal law demands "relevant" licenses, which only exist for certain industries.<sup>94</sup> Additionally, under Minnesota's construction-only law, for a worker to be an independent contractor, the individual must register with the Minnesota Department of Labor and Industry.<sup>95</sup> A former version of Maine's workers' compensation statute also required a contract defining the worker relationship as one of a list of non-dispositive factors.<sup>96</sup> While a solely subjective standard is potentially vulnerable to manipulation, a demand for contracts functionally bans legitimate but informal independent contracting structures; that trade-off is clearly one states have not yet found advantageous outside the construction industry.

The "B" prong shifts attention to the character of the work itself, in relation to the business of the employer, requiring that independent contracting be performed outside the usual course of the employer's business. This prong also has a common variation: four states—Maryland, Nebraska, New Jersey, and Washington—have included an allowance that work performed outside the physical *places* of the employer's business suffices as indicia of independent contracting.<sup>97</sup> Only Nebraska and Washington's statutes are universally applicable (although they only apply under the Workers' Compensation statute, they apply to all industries);<sup>98</sup> the other two only regulate specific industries.<sup>99</sup>

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<sup>91</sup> N.Y. LAB. LAW § 861-c(1)(a) (McKinney 2014); MD. CODE ANN., LAB. & EMPL. §§ 3-902, 3-903 (West 2014).

<sup>92</sup> 43 PA. STAT. ANN. § 933.3(a)(1) (West 2014).

<sup>93</sup> N.M. STAT. ANN. § 60-13-3.1(A)(2) (West 2014).

<sup>94</sup> OR. REV. STAT. ANN. § 670.600(2)(c) (West 2014) (referencing licensing requirements for architects, landscapers, and construction workers).

<sup>95</sup> MINN. STAT. ANN. § 326B.701 subd. 2 (West 2014).

<sup>96</sup> ME. REV. STAT. ANN. tit. 39-A, § 102(13) (2010) (repealed 2011).

<sup>97</sup> MD. CODE ANN., LAB. & EMPL. § 3-903(c) (LexisNexis 2014); NEB. REV. STAT. ANN. § 48-604(5)(b) (LexisNexis 2014); N.J. STAT. ANN. § 34:20-4(b) (West 2014); WASH. REV. CODE ANN. § 50.04.140(1)(b) (West 2014).

<sup>98</sup> NEB. REV. STAT. ANN. § 48-604 (LexisNexis 2014); WASH. REV. CODE ANN. § 50.04.140 (West 2014).

<sup>99</sup> MD. CODE ANN., LAB. & EMPL. §§ 3-902, 3-903(c) (LexisNexis 2014); N.J. STAT. ANN. § 34:20-4 (West

In contrast, the above-mentioned statutes in Pennsylvania, Oregon, and New Mexico have entirely replaced the “B” factor with demands for contracts and licenses.<sup>100</sup> Notably, Pennsylvania provides additional factors including the maintenance of a separate place of business by the independent contractor.<sup>101</sup> In many industries, such as construction, but also trucking and delivering, as in the high-profile FedEx case, occupations routinely occur outside the employer’s physical place of business.<sup>102</sup> For these workers, treating the physical location of work as a signal of independent contractor status is arguably overbroad and may heighten their vulnerability to misclassification. The contrasting strategies in regulations for the construction industry perhaps illustrate a tension between capturing misclassification in an industry rife with illegal practices and preserving the ability of employers to hire independent contractors legitimately underlying these laws, particularly where profitability demands such structures. Clearly states have weighed these concerns differently, as some enable employers to use independent contractors at other locations while other states have tightened requirements.

Finally, the “C” prong examines the character of the independent contractor herself, requiring that she be “customarily engaged in an independently established trade, occupation, profession, or business,”<sup>103</sup> arguably the prong most likely to narrow legitimate independent contracting. States have most drastically altered this prong from the classic model. In Massachusetts and Maryland, the prong’s demands are uniquely heightened, with a requirement that such work also be “of the same nature as that involved” in the service performed.<sup>104</sup> This prong’s analysis particularly necessitates subjective interpretation, introducing complexity as courts use common law factors to apply the formulation to an individual worker. This outcome is apparent in Washington, where courts, at least in the unemployment context, have analyzed the presence of an independently established business by citing to a seven-factor test first set out in 1993.<sup>105</sup> In *Affordable Cabs v. Department of Employment Security*, the state’s court of appeals found a taxicab driver to be an employee because he had not “solicited, advertised, or otherwise held himself out to the community as being in a separate business,” had not “established himself as a separate business . . . [,] did not own his taxi, records, or customer lists,” and “could not continue his business” without the relationship to the employer.<sup>106</sup> These factors are beneficial to workers in their objectivity and longevity. However, judicial explication of statutory language

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2014).

<sup>100</sup> See 43 PA. STAT. ANN. § 933.3 (West 2014); OR. REV. STAT. ANN. § 670.600 (West 2014); N.M. STAT. ANN. § 60-13-3.1(A) (West 2014).

<sup>101</sup> 43 PA. STAT. ANN. § 933.3(b) (West 2014).

<sup>102</sup> See Laura Stevens, *Court Says FedEx Drivers Were Employees, Not Contractors*, WALL STREET JOURNAL, (updated Oct. 3, 2014, 8:58 PM), <http://www.wsj.com/articles/court-says-fedex-drivers-were-employees-not-contractors-1412382296>.

<sup>103</sup> See, e.g., WASH. REV. CODE ANN. § 50.04.140(1)(c) (West 2014).

<sup>104</sup> MASS. GEN. LAWS ANN. ch. 149, § 148B(3) (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-903(c)(1)(ii)(2) (LexisNexis 2014).

<sup>105</sup> See, e.g., *Penick v. Emp’t Sec. Dep’t* 917 P.2d 136, 144-45 (Wash. Ct. App. 1996) (listing as indications of an independent business: “(1) worker has separate office or place of business outside of the home; (2) worker has investment in the business; (3) worker provides equipment and supplies needed for the job; (4) the alleged employer fails to provide protection from risk of injury or non-payment; (5) worker works for others and has individual business cards; (6) worker is registered as independent business with state; and (7) worker is able to continue in business even if relationship with alleged employer is terminated”) (citing *Jerome v. State of Washington*, 850 P. 2d 1345, 1348 (Wash. Ct. App. 1993)).

<sup>106</sup> 101 P.3d 440, 445 (Wash. Ct. App. 2004).

undoubtedly generates less consistency and diminishes notice to employers and employees alike.

Presumably in response to this challenge, four states, Maine, New Mexico, Oregon, and Pennsylvania, have codified specific requirements needed to satisfy “C.”<sup>107</sup> Maine’s law entirely replaced the “C” prong with its mandatory criteria.<sup>108</sup> Although the states’ lists are not identical, they feature shared objective characteristics of independent businesses. New Mexico, Oregon, and Pennsylvania all ask for the maintenance of a separate business location.<sup>109</sup> All four states also look for evidence of other business relationships: New Mexico and Oregon consider two or more clients in one year,<sup>110</sup> Pennsylvania allows for a business that is available for other employment,<sup>111</sup> Maine requires the right and opportunity to work for multiple entities at the contractor’s discretion.<sup>112</sup> Finally, all four states also provide for indicia of financial liability, whether framed as financial responsibility,<sup>113</sup> as significant investment,<sup>114</sup> as bearing the risk of losses,<sup>115</sup> or as exposure to liability.<sup>116</sup> These rules lack the simplicity of a plain ABC structure and prevent the expansion of a standard that is applicable across state lines. Still, if effectively communicated to employers and workers, these factors could provide a transparent, consistent, and objective standard of an “independent business” and thus an independent contractor.

### 3. The Role of the Rebuttable Presumption

An initial presumption of employee status has been more implemented than any other form or feature of the ABC test: only two states, Kansas and Maine, chose to omit an explicit or implicit—via mandatory criteria—presumption of employee status from their legislative redefinition of independent contracting.<sup>117</sup> Irrespective of variations in the substantive standards applied to overcome it, the presumption effectively shifts the burden for establishing a legitimate independent contracting relationship from the worker to the employer. By placing the onus on employers to proactively establish their workers as independent contractors, the presumption transforms the assessment of independent contracting status.

Such debates or adjudications must focus not on an after-the-fact placement of a worker into a category of employment or independent contracting, but instead on an employer’s compliance with the independent contracting exception to the rule of employment. The presumption’s universal application provides an efficient hurdle by removing the need to tailor analysis distinctly to well-established business structures such as subcontracting versus more

<sup>107</sup> See ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014); N.M. STAT. ANN. § 60-13-3.1(A) (West 2014); OR. REV. STAT. ANN. § 670.600(3) (2014); 43 PA. STAT. ANN. § 933.3(b) (West 2014).

<sup>108</sup> ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014).

<sup>109</sup> See N.M. STAT. ANN. § 60-13-3.1(A)(6) (West 2014); OR. REV. STAT. ANN. § 670.600(3)(a) (2014); 43 PA. STAT. ANN. § 933.3(b)(4) (West 2014).

<sup>110</sup> N.M. STAT. ANN. § 60-13-3.1 (West 2014); OR. REV. STAT. ANN. § 670.600(3)(c) (2014).

<sup>111</sup> 43 PA. STAT. ANN. § 933.3(b)(5)(ii) (West 2014).

<sup>112</sup> ME. REV. STAT. ANN. tit. 26, § 1043(11)(E)(1)(a), (c) (2014).

<sup>113</sup> N.M. STAT. ANN. § 60-13-3.1(A)(6)(f) (West 2014).

<sup>114</sup> OR. REV. STAT. ANN. § 670.600(3)(d) (West 2014).

<sup>115</sup> OR. REV. STAT. ANN. § 670.600(3)(b) (West 2014); 43 PA. STAT. ANN. § 933.3(b)(2) (West 2014); ME. REV. STAT. ANN. tit. 26, § 1043(11)(E)(c) (2014).

<sup>116</sup> 43 PA. STAT. ANN. § 933.3(b)(6) (West 2014).

<sup>117</sup> See ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014); KAN. STAT. ANN. § 44-703(i)(3)(D) (West 2014).

unusual business structures, which may have been created by employers trying to circumvent the law. Some argue that for exactly this reason, the presumption's barrier overreaches and blocks legitimate but "unconventional" employment relationships.<sup>118</sup> However, the potency and conceptual directness of the presumption puts employers on notice that in order to lawfully craft novel structures, they must observe independent contracting boundaries.

The presumption can also root out common misclassification tactics, including the establishment of multiple tiers of subcontractors to shift liability and shield a general contractor; a widespread practice in the construction industry.<sup>119</sup> In one illuminating workers' compensation dispute in New York, a window installation general contractor and subcontractor both attempted to evade liability for a worker's on-the-job injury.<sup>120</sup> The state Workers' Compensation Board considered that New York's Construction Industry Fair Play Act, which enacted a presumption and ABC test, did not apply because the worker was injured prior to the implementation of the Act.<sup>121</sup> The board explicitly noted that under the Act the presumption would have established an employer-employee relationship; instead, under the prior law, the board found an employee relationship to the uninsured subcontractor.<sup>122</sup> The decision partly turned on the subcontractor aligning with the general contractor to argue that the worker was an independent contractor, rather than arguing that the subcontractor and worker were both employees of the general contractor.<sup>123</sup> The incentives are clear: if the subcontractor can simultaneously maintain its bottom line and preserve its business relationship with the general contractor, there is no reason to argue that a worker has an employee relationship to either entity.

In contrast, a presumption of employment would have shifted that burden, by forcing the general contractor and subcontractor to proactively establish that each subordinate entity was an independent contractor. In turn, the subcontractor would have had to choose between demonstrating that the worker was an independent contractor, or that both the subcontractor and worker shared employee status under the general contractor.<sup>124</sup> In this way, the presumption could be a powerful tool for realigning the interests of workers and subcontractors and for protecting the interests of workers without placing the burden of asserting such claims on their shoulders alone.

#### 4. Impacts of Contrasting Implementation Strategies for Definitional Changes

The efficacy of the presumption and of the ABC definition also rest on the choices states

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<sup>118</sup> E.g., Karen R. Harned, Georgine M. Kryda & Elizabeth A. Milito, *Creating a Workable Legal Standard for Defining an Independent Contractor*, 4 J. BUS. ENTREPRENEURSHIP & L. 93, 102 (2010).

<sup>119</sup> See CARRÉ & WILSON, *supra* note 16, at 8 (noting that employers in the Maine construction industry "appear to engage in misclassification more frequently than the average of employers across all industries").

<sup>120</sup> Clearview Window Installation, No. 2070 7169, 2011 WL 4819616, at \*2-\*3 (N.Y. Workers' Comp. Bd. Aug. 30, 2011).

<sup>121</sup> *Id.* at \*4.

<sup>122</sup> *Id.*

<sup>123</sup> *Id.* at \*3.

<sup>124</sup> Exclusivity rules in workers' compensation statutes also shift these incentives: where present, such a rule limits the remedies available to eligible employees to workers' compensation. Thus, where an injured worker sees the opportunity to make a tort claim, she may have an interest in arguing to be an independent contractor, while the business gains an incentive to argue for employer status. See Steven E. Goren, *The Workers' Compensation Exclusive Remedy Rule and Its Exceptions*, 71 MICH. B.J. 59, 60 (1992) (discussing why the exclusivity of Michigan's workers' compensation remedy does not apply to independent contractors).

have made about the scope and scale of their application, rather than solely on the simplicity and strength of the presumption and the factors. No state has implemented a universally applicable ABC test and presumption for all workers and across all statutes governing employee-relevant benefits and legal obligations, such as taxes, wage and hour laws, unemployment insurance, and workers compensation. Only three states—Maine, New Hampshire, and Oregon—have legislated regarding all workers.<sup>125</sup> Maine’s change applied only to its workers’ compensation and unemployment insurance,<sup>126</sup> but the state made its laws consistent with preexisting standards in other statutes, creating a matching standard across all laws. Nine states have made definitional changes that only regulate the construction industry,<sup>127</sup> with one additional state regulating only the construction and landscaping industries.<sup>128</sup> Finally, Utah passed legislation to presume certain entities are employers, but limited its application to solely a subset of independent contracting relevant laws.<sup>129</sup>

The advantages of a uniformly and universally applicable law are clear: if a worker is an independent contractor under one statute and an employee under another, compliance is expensive and complex for employers, enforcement becomes inefficient, and workers are hampered from asserting their eligibility for benefits and protections. In 2009, Maryland Governor Martin O’Malley recognized this barrier when he issued an executive order to create a Joint Enforcement Task Force on Workplace Fraud and directly called for overcoming previous reduced “efficiency and effectiveness” through coordination across agencies, necessitating a uniform test for use by all agencies.<sup>130</sup>

A uniform standard can also enhance political support for legislative reform. In 2012, Maine Governor Paul LePage used the existence of multiple independent contract definitions as the rationale for stating he would introduce legislation to make a presumption and non-ABC test uniform across all statutes and workers.<sup>131</sup> Governor LePage framed his legislation as a pro-business measure, arguing that the existence of conflicting standards had “virtually eliminated the use of independent contractors by some businesses.”<sup>132</sup> Governor LePage said that a single

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<sup>125</sup> See An Act to Standardize the Definition of “Independent Contractor,” 2012 Me. Legis. ch. 643 (West); Act of July 17, 2007, 2007 N.H. Adv. Legis. Serv. ch. 362 (LexisNexis); Act of July 28, 2009, 2009 Or. Laws ch. 845 (West).

<sup>126</sup> ME. REV. STAT. ANN. tit. 26, § 1043(11)(E) (2014) (unemployment); ME. REV. STAT. ANN. tit. 39-A, § 102(13-A) (workers’ compensation).

<sup>127</sup> See 43 PA. STAT. ANN. § 933.3 (West 2014) (“Construction Workplace Misclassification Act”); N.Y. LAB. LAW § 861-c (McKinney 2014) (“New York State Construction Industry Fair Play Act”); NEB. REV. STAT. §§ 48-2903 to 48-2907 (LexisNexis 2014) (“Employee Classification Act”); ME. REV. STAT. ANN. tit. 39-A, § 105-A (2009) (“An Act to Ensure That Construction Workers Are Protected by Workers’ Compensation Insurance”) (amended 2010 & 2012); MINN. STAT. ANN. § 181.723 (West 2014) (“Construction contractors”); DEL. CODE ANN. tit. 19, §§ 3501, 3502 (West 2014) (“Workplace Fraud Act”); N.J. STAT. ANN. § 34:20-1 (West 2014) (“Construction Industry Independent Contractor Act”); 820 ILL. COMP. STAT. ANN. 185/1 to 185/999 (2014) (“Employee Classification Act”).

<sup>128</sup> See MD. CODE ANN., LAB. & EMPL. §§ 3-902, 3-903 (LexisNexis 2014) (“Workplace Fraud Act of 2009”).

<sup>129</sup> UTAH CODE ANN. § 34-28-2 (LexisNexis 2014). Utah had also previously defined independent contractors under its workers’ compensation statute using factors similar to the ABC test, see UTAH CODE ANN. § 34A-2-103(2)(b) (LexisNexis 2014).

<sup>130</sup> See MD. DEP’T OF LABOR, LICENSING AND REGULATION, *supra* note 18, at 8, app. A.

<sup>131</sup> See Mal Leary, *LePage Pledges Legislation to Redefine ‘Employee,’* BANGOR DAILY NEWS (Jan. 23, 2011), <http://bangordailynews.com/2011/01/23/politics/lepage-pledges-legislation-to-define-employee>.

<sup>132</sup> *Id.*

standard would “reduce confusion over who’s eligible” for benefits.<sup>133</sup> A supporter called the bills “‘common-sense’ and ‘business-friendly reforms.’”<sup>134</sup> Democrats and organized labor opposed the change as “weakening” the previous standard in workers’ compensation and unemployment insurance statutes.<sup>135</sup> If replicated, reform driven by the business community could trigger a shift away from the ABC test. A former aide to Governor LePage and local Republican strategist called the change “a national model for reform.”<sup>136</sup> Yet, there is no reason that advocates for the ABC framework could not wield the same strategy in similarly justifying ABC bills by the cost savings of their uniform applicability.

The choice to legislatively change statutory definitions for only the construction industry, or for any other single industry, has more apparent advantages than a definition applicable only to certain benefits. As discussed above, the states that have passed construction-only statutes have frequently applied stringent independent contracting definitions, either the ABC test or additional objective requirements such as contracts and licensing.<sup>137</sup> These statutes have often followed research that identified overrepresentation of the misclassification abuses in the construction industry, making a broader application politically challenging and of debatable necessity.<sup>138</sup> By targeting political capital at the industry widely understood to be the greatest culprit of misclassification, construction industry-only statutes can also serve as functional pilot programs, whose effectiveness can be used as evidence for legislative expansion to all industries. However, a strategy that starts and ends with the construction industry will leave workers unprotected in industries where these harms are less widespread or publically known.

### B. “Enforcement” Statutes and Strategies

Nineteen states have passed legislation strengthening or transforming enforcement against the misclassification of workers, both instead of and in addition to definitional changes to existing statutes.<sup>139</sup> Unlike statutory definitions of independent contracting, there is no dominant

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<sup>133</sup> *LePage Signs Workers Comp, Unemployment Bills*, PORTLAND PRESS HERALD (Apr. 18, 2012), <http://www.pressherald.com/news/LePage-signs-workers-comp-unemployment-bills.html>.

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> *See Dan Demeritt: Responsible Representing Calls for Responsible Criticism*, PORTLAND PRESS HERALD (Oct. 7, 2012), [http://www.pressherald.com/opinion/responsible-representing-calls-for-responsible-criticism\\_2012-10-07.html?pagenum=full](http://www.pressherald.com/opinion/responsible-representing-calls-for-responsible-criticism_2012-10-07.html?pagenum=full).

<sup>137</sup> *See* N.Y. LAB. LAW § 861-c (McKinney 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-903 (LexisNexis 2014); 43 PA. STAT. ANN. § 933.3 (West 2014); N.M. STAT. ANN. § 60-13-3.1 (West 2014); OR. REV. STAT. ANN. § 670.600(2)(c) (West 2014).

<sup>138</sup> *See, e.g.,* DONAHUE, LAMARE, & KOTLER, *supra* note 17, at 4 (estimating that about 15% of New York State’s misclassification occurs in the construction industry).

<sup>139</sup> CAL. LAB. CODE § 226.8 (West 2014); COLO. REV. STAT. § 8-72-114 (2014); CONN. GEN. STAT. ANN. §§ 31-69, 31-69a, 31-288 (West 2014); DEL. CODE ANN. tit. 19, § 3505 (West 2014); 820 ILL. COMP. STAT. ANN. 185/25, /40, /45, /60 (West 2014); IND. CODE ANN. § 22-2-15-2 (West 2014); KAN. STAT. ANN. § 44-719 (West 2014); MD. CODE ANN., LAB. & EMPL. §§ 3-908, 3-909, 3-911 (LexisNexis 2014); MASS. GEN. LAWS ANN. ch. 149, § 27C (West 2014); MINN. STAT. ANN. §§ 181.722, 181.723, 326B.701 (West 2014); NEB. REV. STAT. ANN. § 48-2907 (LexisNexis 2014); N.J. STAT. ANN. § 34-20-5 (West 2014); N.M. STAT. ANN. § 60-13-3.1(C) (West 2014); N.Y. LAB. LAW § 861-e (McKinney 2014); OR. REV. STAT. ANN. § 670.700 (West 2014); 43 PA. STAT. ANN. §§ 933.5, 933.6 (West 2014); UTAH CODE ANN. § 34A-2-110 (LexisNexis 2014); VT. STAT. ANN. tit. 21, §§ 692, 708, 1314a (West 2014); WISC. STAT. ANN. § 103.06 (West 2014).

model for these new laws. Most states increased or instituted civil penalties for misclassification, and several added criminal liability. Wisconsin instituted the power to issue stop-work orders against businesses,<sup>140</sup> and two states, Oregon and Indiana, enacted laws solely to restructure their state agency enforcement process.<sup>141</sup> States appear to be experimenting with a myriad of enforcement tactics, including targeting intentional misclassification, creating private rights of action, and implementing successor liability. Measuring the value of each enforcement tool is challenging, as public records documenting enforcement actions are not readily available and agency reports often provide data on fines without sufficient context for assessment. Still, enforcement statutes have some readily apparent benefits. Unlike definitional changes, assessing penalties does not inherently punish businesses currently in compliance, and thus can avoid shifting the boundary of legal independent contracting and facing the likely higher political stakes of such actions.

### 1. Civil Penalty Increases and the Targeting of Intentional Misclassification

The most common enforcement tactic by state legislatures has been civil penalties for misclassification. In contrast to regimes where the only incentive against misclassifying a worker was the assessment of back taxes or benefits, these penalties do more than “place[] the employer in the same position where he would have been had he properly classified the worker in the first instance.”<sup>142</sup> Seven states have created or increased such penalties for *any* business that violates the statute.<sup>143</sup> Eight states deliver civil penalties to businesses whose violations are intentional, either “willful” or “knowing,” depending on the statute.<sup>144</sup> Further, Wisconsin added penalties for violating a new stop-work order mechanism,<sup>145</sup> while Minnesota implemented a registration scheme for construction industry independent contractors including fines for violators.<sup>146</sup>

Notably, only Vermont and Maryland provide for liability to carry to a successor entity.<sup>147</sup> Vermont’s statute signals that liability can extend to “any successor employer that has one or more of the same principals or corporate officers,”<sup>148</sup> while Maryland applies continued

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<sup>140</sup> WISC. STAT. ANN. § 103.06 (West 2014).

<sup>141</sup> See Act of July 28, 2009, 2009 Or. Laws 845 (West) (enacting OR. REV. STAT. ANN. §§ 670.700, 670.705 (West 2006)) (establishing an “Interagency Compliance Network”); Act of March 25, 2010, 2010 Ind. Legis. Serv. P.L. 110-2010 (West) (enacting IND. CODE ANN. § 22-2-15-1 to 22-2-15-6 (West 2010)) (requiring the Indiana department of labor to develop and implement guidelines and procedures to respond to misclassification complaints).

<sup>142</sup> Buscaglia, *supra* note 40, at 121.

<sup>143</sup> 820 ILL. COMP. STAT. ANN. 185/40 (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 27C(b) (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-908 (Lexis Nexis 2014); NEB. REV. STAT. ANN. § 48-2907 (LexisNexis 2014); N.J. STAT. ANN. § 34:20-5(b) (West 2014); 43 PA. STAT. ANN. § 933.6 (West 2014); VT. STAT. ANN. tit. 21, § 1314a (West 2014).

<sup>144</sup> CAL. LAB. CODE § 226.8 (West 2014) (willful), COLO. REV. STAT. § 8-72-114 (2014) (willful); CONN. GEN. STAT. ANN. § 31-69a (West 2014) (knowing); DEL. CODE ANN. tit. 19, §§ 3503, 3505 (2014) (knowing); KAN. STAT. ANN. § 44-719 (West 2014) (willful or knowing); MD. CODE ANN., LAB. & EMPL. § 3-909 (LexisNexis 2014) (knowing); N.Y. LAB. LAW § 861-e(1) (McKinney 2014) (willful); VT. STAT. ANN. tit. 21, § 708 (2014) (willful).

<sup>145</sup> WISC. STAT. ANN. §§ 103.005(10), 103.06 (West 2014).

<sup>146</sup> MINN. STAT. ANN. § 326B.701 (West 2014).

<sup>147</sup> VT. STAT. ANN. tit. 21, § 708(c) (2014); MD. CODE ANN., LAB. & EMPL. §§ 3-908(d), 3-909(g) (LexisNexis 2014).

<sup>148</sup> VT. STAT. ANN. tit. 21, § 708(c) (West 2014).

liability to “any successor corporation or business entity” with “one or more of the same principals or officers” who is “engaged in the same or equivalent trade or activity.”<sup>149</sup> As such, a company should not be able to merely restructure, reincorporate, or entirely disband when faced with the liabilities of its misclassification practices. Such strategies may sound extreme, but given the already demonstrated propensity for these businesses to break the law, such provisions appear to be a valuable mechanism, though perhaps redundant of existing corporate law.

Many of these statutes arrange fines in two tiers, with a lower fine for the first offense and higher fines for every subsequent offense.<sup>150</sup> Yet, the price of the fines varies widely. A first violation costs only \$500 in Nebraska<sup>151</sup> but as much as \$15,000 in Massachusetts<sup>152</sup> and a second violation can cost \$2,500 in Pennsylvania<sup>153</sup> or \$25,000 in Colorado.<sup>154</sup> Fines between \$1,000 and \$5,000 appear in Colorado, Delaware, Illinois, New Jersey, Pennsylvania, and Vermont.<sup>155</sup> States also include distinct features, such as an explicit indication in Colorado that investigations will assess interest in addition to back taxes<sup>156</sup> and, in Delaware, an additional \$500 per day fine against a business under investigation that fails to provide books and records to the relevant agency.<sup>157</sup>

The use of fines against intentional misclassification, whether “willful” or “knowing,” appears to be a simple mechanism to effectively target penalties at bad actors. This tool additionally can funnel businesses into desired actions that demonstrate their intent not to misclassify workers, perhaps reducing the burden on states to enforce statutes through investigations and audits. In addition, some states deliver payment directly to the worker in cases of intentional misclassification: punitive matching awards of up to \$2,000 to \$4,000 in Illinois and “restitution” in New Jersey.<sup>158</sup>

A few states provide businesses a route to rebut the presumption of an employment relationship, in the process providing information to the state about independent contractors. Maryland’s construction businesses must provide information to workers and collect signatures from independent contractors, while Colorado businesses can seek an advisory opinion from the state’s division of unemployment insurance.<sup>159</sup> In addition, Maryland and Delaware also have the power to assess fines against parties, other than businesses, which knowingly assist misclassification. Delaware and Maryland’s statute includes penalties up to \$20,000 against any

<sup>149</sup> MD. CODE ANN., LAB. & EMPL. §§ 3-908(d), 3-909(g) (LexisNexis 2014).

<sup>150</sup> See, e.g., NEB. REV. STAT. ANN. § 48-2907 (LexisNexis 2014).

<sup>151</sup> *Id.*

<sup>152</sup> MASS. GEN. LAWS ANN. ch. 149, § 27C(b) (West 2014).

<sup>153</sup> 43 PA. STAT. ANN. § 933.6 (West 2014).

<sup>154</sup> COLO. REV. STAT. § 8-72-114(3)(e)(III)(A) (2014).

<sup>155</sup> COLO. REV. STAT. § 8-72-114(3)(e)(III)(A) (2014) (providing minimum fine of \$5,000); DEL. CODE ANN. tit. 19, § 3505(a) (2014) (providing fines ranging from \$1,000 to \$5,000); 820 ILL. COMP. STAT. ANN. 185/40(a) (West 2014) (providing maximum fine of \$1,000 for first violation, \$2,000 for second); N.J. STAT. ANN. § 34:20-5 (West 2014) (providing fines of \$100 to \$1,000 and administrative penalties up to \$5,000); 43 PA. STAT. ANN. § 933.6 (West 2014) (providing maximum administrative penalty of \$1,000 for the first violation and \$2,500 for the second); VT. STAT. ANN. tit. 21 § 1314a(f)(B) (2014) (providing maximum fine of \$5,000).

<sup>156</sup> COLO. REV. STAT. § 8-72-114(3)(e)(II) (2014).

<sup>157</sup> DEL. CODE ANN. tit. 19, § 3505 (2014).

<sup>158</sup> 820 ILL. COMP. STAT. ANN. 185/45 (West 2014) (allowing for putative damages in amount equal to the penalties assessed, which may be double the civil penalties); N.J. STAT. ANN. § 34:20-5(a)(2) (West 2014).

<sup>159</sup> MD. CODE ANN., LAB. & EMPL. § 3-903.1 (LexisNexis 2014); COLO. REV. STAT. § 8-72-114(4) (2014).

knowing assistance as well as knowingly incorporating or forming various business entities to evade liability for employees.<sup>160</sup> Despite these novel tactics, it is unclear the scope of their use or their value on the books without enforcement.

## 2. Criminal Liability

Ten states have also added criminal liability for misclassification to their statutes.<sup>161</sup> Liability often requires intent and tends to be registered as a misdemeanor that is subject to prosecution by the state attorney general, as in New Mexico and New York.<sup>162</sup> However, Connecticut, New Jersey, Illinois, and Utah have made misclassification subject to low-level felonies;<sup>163</sup> in Illinois misclassification is a felony solely when the crime is a repeat violation.<sup>164</sup> Many states provide for a greater penalty for intentional misclassification: for example, both New York and Massachusetts' dramatic laws allow up to \$50,000 fines.<sup>165</sup> Although the use of criminal liability appears on paper to be an aggressive tactic, the actual assessment of criminal penalties is hard to track, as investigations appear to typically be private. New York has most publicly pursued criminal enforcement, under both then-Attorney General Andrew Cuomo and current Attorney General Eric Schneiderman. The number of cases prosecuted has been small, only six in 2009, but the state's Misclassification Task Force has publicized those criminal enforcements.<sup>166</sup> Criminal penalties could, perhaps, be an effective tool for targeting employers whose workforces are entirely off the books and those with large-scale misclassification which are insolvent to pay fines or back taxes and benefits.

## 3. Stop-Work Orders

Six states have created the ability to issue stop-work orders against businesses intentionally failing to comply with the law.<sup>167</sup> In Wisconsin, where the law does not afford businesses a hearing prior to the order taking effect, the tactic is controversial,<sup>168</sup> presumably

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<sup>160</sup> DEL. CODE ANN. tit. 19, § 3505 (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-915 (LexisNexis 2014).

<sup>161</sup> CONN. GEN. STAT. ANN. §§ 31-69, 31-288(g) (West 2014); 820 ILL. COMP. STAT. ANN. 185/45(d) (West 2014); KAN. STAT. ANN. § 44-719 (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 27C(a) (West 2014); N.J. STAT. ANN. § 34:20-5(a)(2) (West 2014); N.M. STAT. ANN. § 60-13-3.1(C) (West 2014); N.Y. LAB. LAW § 861-e(4) (McKinney 2014); 43 PA. STAT. ANN. § 933.5 (West 2014); UTAH CODE ANN. § 34A-2-110 (LexisNexis 2014); VT. STAT. ANN. tit. 21, § 692(c) (West 2014) (violation of stop-work order).

<sup>162</sup> See N.M. STAT. ANN. § 60-13-3.1(C) (West 2014); N.Y. LAB. LAW § 861-e(4) (McKinney 2014).

<sup>163</sup> CONN. GEN. STAT. ANN. § 31-288(g) (West 2014); N.J. STAT. ANN. § 34:20-5(a)(2) (West 2014); 820 ILL. COMP. STAT. ANN. 185/45(d) (West 2014); UTAH CODE ANN. § 34A-2-110(3)(c)(ii)(B), (C) (LexisNexis 2014).

<sup>164</sup> 820 ILL. COMP. STAT. ANN. 185/45(d) (West 2014).

<sup>165</sup> MASS. GEN. LAWS ANN. ch. 149, § 27C(a)(1) (West 2014); N.Y. LAB. LAW § 861-e (McKinney 2014).

<sup>166</sup> N.Y. STATE DEP'T OF LABOR, ANNUAL REPORT OF THE JOINT ENFORCEMENT TASK FORCE ON EMPLOYEE MISCLASSIFICATION 13 (2010) available at <http://www.labor.ny.gov/ui/2010Febreport%20with%20Cover%20to%20Paterson%20and%20Index.pdf>.

<sup>167</sup> See 43 PA. STAT. ANN. § 933.7 (West 2014); WISC. STAT. ANN. § 103.06 (West 2014); CONN. GEN. STAT. ANN. §§ 31-69a, 31-76a (West 2014); VT. STAT. ANN. tit. 21, § 692(b) (West 2014); DEL. CODE ANN. tit. 19, § 3505(b), (f) (West 2014); ME. REV. STAT. ANN. tit. 39-A, § 105-A(5) (2014).

<sup>168</sup> Troy D. Thompson, *Employees vs. Independent Contractors: State Broadens Enforcement of Worker Misclassification Issues*, INSIDE TRACK (Sept. 1, 2010), <http://www.wisbar.org/newspublications/insidetrack/pages/>

because the costs of a closed business quickly outpace the scale of the civil fines. Nonetheless, states are beginning to use stop-work orders as tools: the Connecticut Department of Labor reported that its Stop-Work Unit issued 127 stop-work orders in the year from March 2010 to February 2011 and collected \$38,700 in civil fines from businesses.<sup>169</sup> The state's Joint Enforcement Commission identified the orders as more effectively incentivizing businesses against misclassification than previous penalties, which the state's business community had complained were "insufficient to deter knowing misclassification violations."<sup>170</sup> Stop-work orders are more punitive and more indefinite than monetary penalties, which businesses can calculate and build into their cost model. The costs of stop-work orders are not only monetary but also reputational. The costs of delayed work are also borne by any impacted customers, providing an incentive for customers to negotiate *ex ante* and pay for properly classified workers or to perhaps indicate that the business will shift costs to protect the customer if an order is issued.

#### 4. Enforcement Mechanisms: Coordinated Investigations and Increased Resources

Predictably, the actual impact of many of these increased penalties for employee misclassification is determined by the shape and scale of their enforcement. The heart of misclassification investigations in many states has been the creation and implementation of task forces.<sup>171</sup> Other states have incorporated information sharing and restructuring of multi-agency enforcement into their independent contractor statutes. Indiana is one such state, having passed a statute mandating the sharing of information between agencies about businesses found to misclassify employees.<sup>172</sup> Illinois and Delaware similarly require cooperation and information sharing about businesses suspected of misclassification.<sup>173</sup> Illinois creatively made its independent contracting investigations self-sustainable by allocating all collected civil fines to the statute's administration and its resulting investigations.<sup>174</sup>

#### 5. Enforcement by Workers: Private Rights of Action and Anti-Retaliation Provisions

Finally, six states—Delaware, Illinois, Massachusetts, Maryland, New Jersey, and Washington—have additionally established private rights of action, empowering aggrieved workers to initiate suits against an employer violating the independent contracting statute.<sup>175</sup> In Delaware, a worker may initiate an action only after he has filed a complaint to the state and

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article.aspx?volume=2&issue=17&articleid=7800.

<sup>169</sup> CONN. JOINT ENFORCEMENT COMM'N ON EMP. MISCLASSIFICATION, *supra* note 23, at 2.

<sup>170</sup> *Id.*

<sup>171</sup> *See, e.g.*, MD. DEP'T OF LABOR, LICENSING AND REGULATION, *supra* note 18, at 2; MD. DEP'T OF LABOR, LICENSING AND REGULATION, ANNUAL REPORT OF THE JOINT ENFORCEMENT TASK FORCE ON WORKPLACE FRAUD 4 (2011), available at <http://www.dllr.maryland.gov/workplacefraudtaskforce/wpftfannrep2011.pdf> (reporting that over \$600,000 had been paid into the state's unemployment trust fund from fraud audits).

<sup>172</sup> IND. CODE ANN. § 6-8.1-3-21.2(c) (West 2014).

<sup>173</sup> DEL. CODE ANN. tit. 19 § 3507 (West 2014); 820 ILL. COMP. STAT. ANN. 185/75 (West 2014).

<sup>174</sup> 820 ILL. COMP. STAT. ANN. 185/50 (West 2014).

<sup>175</sup> DEL. CODE ANN. tit. 19, § 3508 (West 2014); 820 ILL. COMP. STAT. ANN. 185/60 (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 150 (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-911 (LexisNexis 2014); N.J. STAT. ANN. § 34:20-8(b) (West 2014); WASH. REV. CODE ANN. § 49.44.170(3) (West 2014).

ninety days have passed without state investigation.<sup>176</sup> However, the interest of states in inviting employee reports to be part of their enforcement schemes is perhaps suspect. Explicit anti-retaliation provisions in four states—Delaware, Illinois, New York, and Vermont—protect workers who complain of misclassification to an agency or file a lawsuit complaining of misclassification.<sup>177</sup> Illinois also allows for “[a]ny interested party” to either file suit or to file a complaint with the state if that party has a “reasonable belief” that the employer is violating the statute.<sup>178</sup> Considering the competitive harm that misclassification does to businesses who comply with the law, this mechanism could provide a valuable tool for compliant businesses to enforce misclassification laws against noncompliant businesses, providing additional buy-in to the legislation and empowering private actors possessing more resources than workers to assist in enforcement.

### III. EMPLOYER ATTEMPTS TO EVADE MISCLASSIFICATION LAWS IN ADJUDICATIONS

With the passing of these stricter independent contractor statutes, some employers have developed new strategies to avoid liability for misclassification. This Part will provide an analysis of how these statutes are faring against such strategies in adjudications. We focus on the successes and weaknesses of the ABC test, as it is the most common test used in recent legislation. This test, or a variation of it, is employed by fourteen of the sixteen states that have changed the statutory definition of independent contractor.<sup>179</sup> Where courts have failed to provide an adequate response to employer strategies, we will suggest alternative arguments for workers and enforcement agencies, as well as legislative solutions.

Because many of the independent contractor misclassification statutes have passed within recent years, this discussion is preliminary. We will concentrate largely on adjudications in Massachusetts and Washington, where the statutes are older and not industry specific, providing more opportunity for litigation. This discussion will include cases litigated under Washington’s Unemployment Insurance independent contractor definition, an ABC statute enacted in 1991.<sup>180</sup> This statute’s age in particular has allowed ample time for significant case law to develop. While impediments to holding employers liable for misclassification are not necessarily widespread, they may become more pervasive. In some cases, these new strategies may lead employers further from the reach of the law, as some engage in tactics the law does not yet condemn. We do not attempt to document every argument or tactic, but instead focus on common approaches used by employers, including the use of subcontracting, misclassification of workers as business entities,

<sup>176</sup> DEL. CODE ANN. tit. 19 § 3508(a) (West 2014).

<sup>177</sup> 820 ILL. COMP. STAT. ANN. 185/55 (West 2014); DEL. CODE ANN. tit. 19, § 3509 (West 2014); VT. STAT. ANN. tit. 21, § 710(d) (2014); N.Y. LAB. LAW § 861-f (McKinney 2014).

<sup>178</sup> 820 ILL. COMP. STAT. ANN. 185/25 (West 2014).

<sup>179</sup> DEL. CODE ANN. TIT. 19, § 3501 (West 2014); 820 ILL. COMP. STAT. ANN. 185/10 (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-903 (LexisNexis 2014); MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014); MINN. STAT. ANN. § 181.723 (West 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014) (referencing NEB. REV. STAT. ANN. § 48-604(5)(a) (LexisNexis 2014)); N.H. REV. STAT. ANN. § 275:4 (2014); N.J. STAT. ANN. § 34:20-4 (West 2014); N.M. STAT. ANN. § 60-13-3.1 (West 2014); N.Y. LAB. LAW § 861-c (McKinney 2014); OR. REV. STAT. ANN. § 670.600 (West 2014); 43 PA. STAT. ANN. § 933.3 (West 2014); UTAH CODE ANN. § 34A-2-103 (LexisNexis 2014); WASH. REV. CODE ANN. § 50.04.140 (West 2014). *Cf.* KAN. STAT. ANN. § 44-703 (West 2014); ME. REV. STAT. ANN. tit. 39-A, § 102(13-A) (2014).

<sup>180</sup> WASH. REV. CODE ANN. § 50.04.140 (West 2014).

and the common exploitation of semantic distinctions to claim that a worker meets the elements of the independent contractor test.

Before exploring employer attempts to evade these new laws, it important to note that not every employer is responding to stricter laws by trying to exploit their weaknesses. Many businesses already classify workers correctly as employees, and others are now reclassifying their independent contractors as employees in response to these new laws.<sup>181</sup> Additionally, many law firms are advising clients to classify correctly.<sup>182</sup> The recent wave of legislation has not solely pushed employers further outside the reach of the law, but has also encouraged many employers to comply.

#### *A. New Misclassifications: Workers as Business Entities*

One strategy that some employers have used to avoid liability under stricter independent contractor misclassification statutes is to reclassify their independent contractors not as employees, but as business entities. This tactic may prevent employers from being held liable for misclassification because some state laws provide that corporations cannot be employees,<sup>183</sup> while others fail to address whether different corporate forms can be considered employees.<sup>184</sup> By classifying workers as business entities, employers can contract with an independent business or

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<sup>181</sup> See COMMONWEALTH OF MASS., JOINT ENFORCEMENT TASK FORCE ON THE UNDERGROUND ECONOMY AND EMPLOYEE MISCLASSIFICATION, 2011 ANNUAL REPORT 1 (2011), <http://www.mass.gov/lwd/eolwd/jtf/annual-report-2011.pdf> (“The majority of Massachusetts employers pay their applicable taxes, classify their workers legally, and contribute in a responsible manner as a part of our economy and as members of the community.”); Renee Inomata, *Perils of Misclassification of Workers as Independent Contractors*, in INSIDE THE MINDS: COMPLYING WITH EMPLOYMENT REGULATIONS 23 (2012), available at 2012 WL 3279180, at \*6 (“[C]osts of class actions are driving decisions by employers to reclassify workers as employees and to seek prompt and private resolutions of misclassification allegations.”); WASH. STATE DEP’T OF LABOR & INDUS., 2010 ANNUAL FRAUD REPORT TO THE LEGISLATURE 14 (2010) (finding approximately three percent of businesses reclassified workers after being educated about new independent contractor definitions).

<sup>182</sup> See Inomata, *supra* note 181, at \*7 (“In the ever-changing world of employment regulations, counsel and clients alike should proactively take reclassification efforts seriously to avoid having to defend actions by government agencies and class action lawyers.”); Sharon L. Davis & Gregory S. Galaida, *Misclassification of Workers: “Saving Money” Can Be Very Costly*, 39-DEC COLO. LAW. 57, 57 (Dec. 2010) (“Given the potential for liability, employers must be extra vigilant with respect to classification of workers as independent contractors.”); Vaughn Burkholder & Tara Eberline, *Misclassification of Workers as Independent Contractors*, 18 NO. 2 KAN. EMP. L. LETTER 1 (May 2011) (“Because of the increased scrutiny on worker misclassification, employers must be extra vigilant to make sure their workers are properly classified.”); Scott Holt, *Will ‘Misclassification Initiatives’ Reduce Employers’ Use of Independent Contractors?*, 15 NO. 4 DEL. EMP. L. LETTER 6 (Apr. 2010) (encouraging employers who employ independent contractors to conduct internal audits and reviews of worker classifications); Kevin Sullivan, *Paying Workers as Independent Contractors? Better Think Twice*, 22 NO. 4 CAL. EMP. L. LETTER 4 (May 21, 2012) (urging California businesses to seek counsel to determine if workers are properly classified under California law); Jasmin M. Rojas, *Misclassification Can be Costly—and Unfair!*, 23 NO. 7 MASS. EMP. L. LETTER 3, (Oct. 2012) (“As a result of the intense scrutiny in this area, you should review your practices and double-check to make sure you aren’t inadvertently misclassifying employees.”); Robert C. Nagle, *Employers Facing Increased Scrutiny Over Worker Classification*, 20 NO. 9 PA. EMP. L. LETTER 1 (June 2010) (encouraging employers to review and audit worker classifications).

<sup>183</sup> See, e.g., MINN. STAT. ANN. § 181.723 (West 2014) (stating that individuals will be presumed to be employees unless they meet certain criteria, and defining the term “individual” as “a human being”).

<sup>184</sup> See, e.g., MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014) (stating that individuals performing any service will be considered employees unless they meet certain criteria, without defining the term “individual”).

limited liability corporation, instead of an individual worker. Employers sometimes also classify workers as franchisees, partners or owners of the employers' own business. This Part will provide an overview of this strategy, potential solutions, and a discussion of employers' ability to utilize this tactic under different statutory schemes.

At first brush, it seems logical to prevent a worker from being considered an employee if the worker is in fact the owner of his or her own independent business. Indeed, this is one scenario where the independent contractor designation was intended to apply.<sup>185</sup> However, in some instances, employers contract with workers as owners, franchisees, or partners to explicitly avoid worker protections and tax obligations that come with employee status, when these workers are not actually franchisees, partners, or owners of anything more than a shell corporation. In some cases, employers have conditioned hiring a worker on the worker obtaining a business license.<sup>186</sup> Other employers have unsuccessfully argued that the worker is actually a partner in the employer's own business.<sup>187</sup> After the misclassification statute was passed in Minnesota, there was an increase in workers forming limited liability corporations.<sup>188</sup> This increase was specifically noted in the construction industry, the only industry covered by the statute.<sup>189</sup> Similarly, in 2011 Utah initiated seventy-five enforcement actions against employers who misclassified workers as owners in the employers' limited liability corporation.<sup>190</sup> These employer tactics have the same purpose as misclassifying employees as independent contractors; employers are merely using new labels to achieve the same results. As stated by Utah's Deputy Commissioner of the Labor Commission, Alan Hennebold, "we will see individuals who are clearly employees called independent contractors. Now, we're seeing them called members of LLCs. The beat goes on."<sup>191</sup>

To make matters worse, companies have emerged to assist employers in assembling these new classifications to avoid liability under new independent contractor statutes.<sup>192</sup> For example, in Utah, there are businesses that help employers classify workers as owners of limited liability corporations.<sup>193</sup> One such company, U&I LLC, helps employers classify their own workers as owners in U&I LLC.<sup>194</sup> U&I LLC advertises that this will help companies save on labor costs, such as unemployment, workers compensation and payroll taxes.<sup>195</sup> U&I LLC also

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<sup>185</sup> See, e.g., Carlson, *supra* note 34, at 297 ("[I]ndependent contractors' are clearly employers or business owners in their own right and are not employees of the persons they serve.").

<sup>186</sup> See *Kabrick v. Emp't Sec. Dep't*, No. 20126-1-III, 2002 WL 91270, at \*2 (Wash. Ct. App. Jan. 24, 2002) ("Spokane Cab required its drivers to obtain independent business licenses before being allowed to drive for them.").

<sup>187</sup> See *Leffler v. Dep't of Labor & Indus.*, No. 63900-5-I, 2009 WL 3419587, at \*4-5 (Wash. Ct. App. Oct. 26, 2009) (finding construction workers were not partners in the employer's business); *Penick v. Emp't Sec. Dep't*, 917 P.2d 136, 143-45 (Wash. Ct. App. 1996) (finding truck drivers were employees and not participants in joint ventures).

<sup>188</sup> ADVISORY TASK FORCE ON EMP. MISCLASSIFICATION, REPORT TO THE 2011-2012 BIENNium, EIGHTY-SEVENTH LEGISLATURE 8 (2011), available at <http://archive.leg.state.mn.us/docs/2011/mandated/110509.pdf>.

<sup>189</sup> *Id.*

<sup>190</sup> UTAH WORKER CLASSIFICATION ENFORCEMENT COUNCIL, ANNUAL REPORT 3-4 (2011), available at <http://laborcommission.utah.gov/media/pdfs/laborcommission/pubs/AnnualReport2011final.pdf>.

<sup>191</sup> Lori Prichard, *KSL 5 News Investigates Potential Worker Misclassification in Construction Industry*, KSL.COM, (Mar. 26, 2010), <http://www.ksl.com/?nid=148&sid=10934339>.

<sup>192</sup> *Id.*

<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

<sup>195</sup> *Id.*

advertises that this system will still allow employers to exert control and provide direction to their worker-owners,<sup>196</sup> a benefit employers would have to sacrifice if they correctly classified their workers as independent contractors. Another company, CSG Workforce, which appears to no longer be in business,<sup>197</sup> at one point had 1,500 “member owners,” or workers, that were classified as owners in its company.<sup>198</sup> After being re-classified, these workers worked largely in the same capacity.<sup>199</sup> Such tactics have harmed workers and state coffers by providing a mechanism that enables employers to avoid paying benefits, payroll taxes, and workers compensation insurance.<sup>200</sup> The negative impact does not fall solely on workers: companies that do comply with classification statutes have expressed concern over the impact these tactics have had on their ability to compete in the marketplace.<sup>201</sup>

### 1. The Impact of Different Statutory Models on Employers’ Ability to Exploit a Worker’s Business Status

Misclassification of workers as business entities has already arisen in court adjudications, and the result the court reaches may depend on the state’s statutory scheme. Some states’ statutes are silent as to whether a corporation can be considered an employee.<sup>202</sup> Other state employment laws, including but not limited to the independent contractor statute itself, however, may specifically exempt corporations from being considered employees.<sup>203</sup> Similarly, some courts have interpreted ambiguous employment statutes to mean that corporations cannot be employees.<sup>204</sup> For states in these latter categories, it will be more difficult for workers to argue that they are employees who have been misclassified as business entities.

However, where courts simply apply the ABC test to determine whether a worker is an independent contractor, regardless of whether the worker was working in her individual capacity or under the name of a corporation, the ABC test sufficiently protects both employers and employees: it protects employers from having true business entities classified as employees, and

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<sup>196</sup> *Id.*

<sup>197</sup> See *BBB Business Review: CSG Workforce Partners LLC*, BETTER BUS. BUREAU <http://www.bbb.org/utah/business-reviews/contractors-general/csg-workforce-partners-in-provo-ut-22232962> (last visited Jan. 22, 2015).

<sup>198</sup> Prichard, *supra* note 191.

<sup>199</sup> See, e.g., *id.* (“Even though one would expect an ‘owner’ to have influence over their workday, Delgado [who was classified as a member owner of CSG Workforce] says he still took orders from the same contractors. He was occasionally ordered to work six days a week, which job site to report to and what exactly to do.”).

<sup>200</sup> See *id.*

<sup>201</sup> See *id.*

<sup>202</sup> See, e.g., MASS. GEN. LAWS ANN. ch. 149, § 148B (2014) (stating that individuals performing any service will be considered employees unless they meet certain criteria, without defining the term “individual”).

<sup>203</sup> See, e.g., MINN. STAT. ANN. § 181.723 (West 2014) (stating that individuals will be presumed to be employees unless they meet certain criteria, and defining the term “individual” as “a human being”).

<sup>204</sup> *Tvedt v. Farmers Ins. Group of Cos.*, 91 P.3d 1, 11 (Mont. 2004) (interpreting the definition of employment in Montana’s labor code to prevent a corporation from being an employee of another corporation); *Stellar Ins. Group, Inc. v. Cent. Cos.*, No. 2:06cv11, 2006 WL 2862218, at \*9 (W.D.N.C. Sept. 12, 2006) (“Plaintiff Stellar, cannot allege a cause of action under North Carolina’s Wage and Hour Act inasmuch as a ‘corporation’ cannot be an ‘employee’ or wage earner.”); *Frank Burns, Inc. v. Interdigital Commc’ns Corp.*, 704 A.2d 678, 680 (Pa. Super. 1997) (finding that a corporation cannot be an employee under Pennsylvania’s Wage Payment and Collection Law).

employees from being misclassified by the courts as independent contractors. In a recent case in Massachusetts, a state whose statute does not explicitly state whether a corporation can be considered an employee, a court did find that one corporate structure, franchisees, could be considered employees.<sup>205</sup> In making this determination, the court in *Awuah v. Coverall North America, Inc. (Awuah I)* applied Massachusetts's independent contractor statute to the facts of the case without discussing whether the statute applied to franchisees.<sup>206</sup> The franchisee plaintiffs had entered into a contract to purchase janitorial cleaning franchises from defendant Coverall.<sup>207</sup> Until May 2009, customer contracts were with Coverall, and unless a customer specifically requested it, franchisees could not be parties to these contracts.<sup>208</sup> In addition, each time the plaintiffs cleaned for a customer, the customer paid Coverall directly.<sup>209</sup> The court found that Coverall had misclassified the plaintiffs because Coverall was unable to establish that the plaintiffs performed services outside of the course of Coverall's business; the second prong of the ABC inquiry.<sup>210</sup> To prove this prong, Coverall needed to show that the plaintiffs were performing services as part of their own business that was independent from Coverall's business.<sup>211</sup> The court determined that like the plaintiff franchisees, Coverall was in the business of selling cleaning services because it directly received fees for each service, was a party to each customer contract until May 2009, trained the franchisees, and provided them with uniforms.<sup>212</sup>

In applying the second prong of the ABC test, the court analyzed whether the workers were truly distinct business entities, working in independent businesses outside of the course of Coverall's business, or whether the franchisee title was merely an empty label.<sup>213</sup> Thus, the ABC test is sufficient to distinguish between employees and business owners who are performing distinct services for the employer through their own independent businesses, because this specific inquiry is written into the independent contractor test. True business entities should meet each element, and be classified as independent contractors. States that prevent corporations from being employees are adding an additional, unnecessary layer of protection for employers, leaving workers unprotected from this form of misclassification.

The *Awuah I* decision may have closed a loophole that was open for years. According to a recent article, *Awuah* "has rocked a significant sector of the U.S. economy that has always thought franchise arrangements were immune to employee misclassification claims."<sup>214</sup> It is unclear whether other states will follow the lead of the Massachusetts court in *Awuah* and find that franchisees can be misclassified. At the very least, *Awuah I* has influenced law firm advice to

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<sup>205</sup> *Awuah v. Coverall N. Am., Inc.*, 707 F. Supp. 2d 80, 85 (D. Mass. 2010).

<sup>206</sup> *Id.*

<sup>207</sup> *Id.* at 82.

<sup>208</sup> *Id.*

<sup>209</sup> *Id.* at 82, 84.

<sup>210</sup> *Id.* at 84.

<sup>211</sup> *Id.* at 82.

<sup>212</sup> *Id.* at 84.

<sup>213</sup> *See id.* at 82. ("To satisfy the second prong, Coverall must establish that the worker 'is performing services that are part of an independent, separate, and distinct business from that of the employer.'") (quoting *Am. Zurich Ins. Co. v. Dep't of Indus. Accidents*, No. 053469A, 2006 WL 2205085, at \*4 (Mass. Super. June 1, 2006)).

<sup>214</sup> Rochelle B. Spandorf, *Who's the Boss? Franchisors Must Be Able to Demonstrate the Separate and Distinct Businesses That They and Their Franchisees Operate*, L.A. LAW., Mar. 2011, at 18, 18; *see also* W. Michael Garner, *Employment Relationships*, in 1 FRANCHISE & DISTRIBUTION LAW & PRACTICE § 1:30 (2013) ("In 2010, franchise practitioners were surprised to learn that a court had ruled a franchised business to be an employee of the franchisor.").

employers. This same article advised California practitioners to focus on assisting franchisor clients in reducing liability for such misclassification.<sup>215</sup>

Other states have also considered evidence that a worker owns a business as a factor in determining whether the worker is an independent contractor, without letting such labels end the inquiry. For example, in *Western Ports Transportation, Inc. v. Employment Security Department of the State of Washington*, although the worker, Mr. Marshall, contracted with his employer under his business's name, the court still found that he was an employee.<sup>216</sup> The court determined that Marshall was not free from his employer's control because he was required to keep his truck clean, to obtain his employer's permission before transporting passengers, and to go to the dispatch center to obtain assignments that had not been scheduled in advance.<sup>217</sup> Additionally, he could be terminated for any violation of written company policy.<sup>218</sup> Thus, the employer failed to satisfy the first prong of the ABC test, and Marshall was found to be an employee.<sup>219</sup> The court also noted that his business was unrelated to the work he was performing for the company as a truck driver.<sup>220</sup> Ultimately, case law suggests that thus far, the ABC test allows courts to look beyond labels and evaluate whether workers are truly engaged in a separate business or whether the business is being used by the employer to evade wage, tax, and other obligations.

However, where a state's statutory scheme explicitly exempts corporate forms from being considered employees, a court may be unable to evaluate whether the worker is operating a distinct business. In *Nelson v. Levy*, the Minnesota Court of Appeals found that plaintiff Nelson's Limited Liability Corporation, C. Nelson Tile Installation, could not be considered an employee of Majestic Tile & Stone, LLC under Minnesota's construction-specific independent contractor statute.<sup>221</sup> The Minnesota statute presumes that *individuals* who perform services for a person are employees, and defines an "individual" as "a human being."<sup>222</sup> At the time the case was decided, the statute required such individuals to obtain an independent contractor exemption certification to overcome the employee presumption.<sup>223</sup> Because the statute defines individual as "a human being," the court reasoned that under the plain statutory language, C. Nelson Tile Installation, as an LLC, could not obtain such an exemption.<sup>224</sup> The court then determined that it had two choices; it could either automatically find LLCs in the construction industry to always be employees, or it could conclude that the distinction between employees and independent contractors was inapplicable to LLCs in the construction industry.<sup>225</sup> It chose the latter, holding that "an LLC is not the employee of another entity."<sup>226</sup> As a result of *Nelson*, any employer in the Minnesota construction industry can require workers to create their own limited liability corporations as a condition of employment, to avoid the requirements of Minn. Stat. § 181.723,

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<sup>215</sup> Spandorf, *supra* note 214.

<sup>216</sup> *W. Ports Transp., Inc. v. Emp't Sec. Dep't of Wash.*, 41 P.3d 510, 514, 520 (Wash. Ct. App. 2002).

<sup>217</sup> *Id.* at 517-18.

<sup>218</sup> *Id.* at 518.

<sup>219</sup> *Id.* at 520.

<sup>220</sup> *Id.* at 514.

<sup>221</sup> *Nelson v. Levy*, 796 N.W.2d 336, 342-43 (Minn. Ct. App. 2011).

<sup>222</sup> MINN. STAT. ANN. § 181.723 (West 2014).

<sup>223</sup> MINN. STAT. ANN. § 181.723 subdiv. 4 (West 2011) (amended 2012).

<sup>224</sup> *Nelson*, 796 N.W.2d at 342.

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* at 342-43.

and to avoid paying these worker-owners the minimum wage or overtime, and paying the state unemployment, workers compensation and payroll taxes. Although some state statutes punish knowing or willing misclassification, if the independent contractor distinction simply does not apply, such intentional flaunting of the law is technically legal. Thus, depending on the exact statute, it is currently possible for employers to successfully skirt misclassification laws by inducing workers to form LLCs and changing their classification of workers from independent contractor to owners of an LLC.

## 2. Recommendations

There are potential remedies available to prevent employers from using this strategy to avoid liability under misclassification statutes, even for workers in states with statutory language that expressly prohibits corporations from being classified as employees. The best solution would be a clear statutory amendment that expands the presumption of employee status to include any person, partner, owner, or any corporate form or business entity. However, until such amendments are made, there are common law solutions available to worker plaintiffs and enforcement agencies. Some of these remedies have been untested in the context of independent contractor misclassification. Other remedies that will be suggested are based on limited case law. As a result, the likelihood of succeeding in these arguments cannot be predicted with certainty. Accordingly, the limitations of each argument will be discussed.

### i. Statutory Amendments

Most independent contractor statutes do not explicitly extend the presumption of employee status to all workers who are business entities. An amendment to current independent contractor statutes that expands the definition of “individual” to include any person, partner, owner, or any corporate entity would provide the most protection from misclassification. Employers would still be able to prove that a worker’s work was performed as a part of its own independent business venture, but employers who force workers into forming their own businesses would be punished for misclassification. Although the ambiguous statutes in Washington and Massachusetts have led to some favorable court decisions, such statutes still leave room for courts to find that the statute precludes corporations from being employees. Thus, amendments to current statutes that cure ambiguity would allow workers and employers to avoid extensive litigation in the courts. Both workers and employers would know *ex ante* whether the misclassification statute applies to their relationship, reducing uncertainty over classification, a benefit to both workers and employers.

Some states with more recent statutes or statutory amendments have taken steps to try to close this loophole. However, most of these statutes or statutory amendments do not cover every employer or every potential form of misclassification. For example, Utah recently passed amendments clarifying that construction companies that are required to be licensed will be presumed to be the employer of all individuals who hold an ownership interest in their company.<sup>227</sup> However, the statute only applies to unincorporated employers, and will only protect

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<sup>227</sup> See Construction Licensees Related Amendments, 2011 Utah Laws ch. 413 (amending UTAH CODE ANN. § 34-28-2 to define “unincorporated entity” and create a presumption of employer status). For a listing of construction businesses required to be licensed under Utah Law, see UTAH CODE ANN. § 58-55-301 (LexisNexis 2014).

workers who are classified as owners in the *employer's* own company.<sup>228</sup>

Similarly, Delaware's independent contractor statute, while an improvement, still does not provide enough protection for workers. The statute makes it a violation to:

[K]nowingly incorporate or form, or assist in the incorporation or formation of, a corporation, partnership, limited liability corporation, or other entity, or pay or collect a fee for use of a foreign or domestic corporation, partnership, limited liability corporation, or other entity for the purpose of facilitating, or evading detection of, a violation of this section.<sup>229</sup>

Because it may be difficult for plaintiffs to prove that the employer's conduct was knowing, the Delaware statute would be stronger if it presumptively labeled all corporate forms as employees, rather than solely imposing liability for such incorporation where the misclassification is intentional.

New York's statute states that a person will be presumed to be an employee unless it is a "separate business entity," including "any sole proprietor, partnership, corporation or entity that may be a contractor."<sup>230</sup> However, a person will only be considered a "separate business entity" when the entity meets twelve criteria listed in the statute.<sup>231</sup> These criteria include that the business entity has substantially invested capital in the entity beyond equipment and a vehicle, regularly makes its services available to the general public, and regularly has the right to perform such services when it chooses.<sup>232</sup> Thus, in contrast to the other statutes, the New York statute covers all business entities and the criteria listed would seem to prevent a worker who is merely a shell corporation from being considered an independent contractor.<sup>233</sup> However, this statute is limited in scope as it only applies to the construction industry.<sup>234</sup> A statute modeled after the New York statute that is applicable to all industries should protect workers from being misclassified as business entities.

## ii. Alter Ego Liability

Even without legislative reform, workers and enforcement agencies can use the theory of alter ego liability to argue that courts should ignore these corporate forms, and still apply the independent contractor definition to determine whether the plaintiff is an employee. Under alter

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<sup>228</sup> UTAH CODE ANN. § 34-28-2(2)(a) (LexisNexis 2014) ("[a]n unincorporated entity that is required to be licensed under Title 58, Chapter 55, Utah Construction Trades Licensing Act, is presumed to be the employer of each individual who, directly or indirectly, holds an ownership interest in the unincorporated entity"); *see also* 820 ILL. COMP. STAT. ANN. 185/10 (West 2014) (extending the presumption of employee status to sole proprietors and partnerships, but failing to expressly include other business entities in this presumption).

<sup>229</sup> DEL. CODE ANN. tit. 19, § 3503(d) (West 2014).

<sup>230</sup> N.Y. LAB. LAW § 861-c (McKinney 2014).

<sup>231</sup> *Id.* § 861-c(2).

<sup>232</sup> *Id.*

<sup>233</sup> For another example of a statute that explicitly allows business entities to be employees see OR. REV. STAT. ANN. § 670.600(5)(a) (West 2014) ("The creation or use of a business entity, such as a corporation or a limited liability company, by an individual for the purpose of providing services does not, by itself, establish that the individual provides services as an independent contractor.").

<sup>234</sup> N.Y. LAB. § 861-c (McKinney 2014).

ego liability, a court disregards corporate entity status when that entity is shown to be a fiction or a mere instrumentality for another corporation.<sup>235</sup> For example, alter ego liability exists when a company perpetrates fraud by claiming to do business with another ostensibly separate corporation, when in fact the second corporation is a merely a conduit for the company.<sup>236</sup> Applying this theory to the misclassification context, if the fictitious corporation (here, the worker) is found to be in fact inseparable from the employer's company, the court can disregard that fictitious entity and hold the employer liable for its use of the worker's corporate classification to avoid proper worker classification. Different states employ distinct factors to determine whether one company or individual is the alter ego of another, but common factors include undercapitalization, failure to follow statutory incorporation formalities, and neglect of corporate requirements such as the holding of regular shareholder or director meetings.<sup>237</sup>

Although this theory has been applied in the labor and employment context,<sup>238</sup> it is not yet commonly used in suits for misclassification of independent contractors. It thus remains unclear whether the theory could be successfully used to hold employers liable for misclassification. The general rule that corporate entity status can be discarded under alter ego liability is justified as an exception to the policy goal of allowing limited liability through incorporation.<sup>239</sup> As a result, it may be difficult for plaintiffs to prove that this rare exception should be applied in the independent contractor context. Still, plaintiffs have a strong argument that the rationale behind limited liability is inapplicable in the worker-owner misclassification context. The general notion of "piercing the corporate veil" exists because it is "unjust to permit those who control companies to treat them as single or unitary enterprises and then assert their corporate separateness in order to commit frauds and other misdeeds with impunity."<sup>240</sup> If the worker's incorporation were appropriate, it should be undertaken to provide the worker with limited liability. Under this logic, the alter ego doctrine may be applicable where workers' business entities have no purpose beyond helping their employer avoid tax liability and compliance with wage laws. If litigants can demonstrate that the purpose of a worker's incorporation is in fact to shield the employer, it would likely justify an exception to the general preference of preserving corporate entities and allow a court to hold the employer liable for misclassification.

Yet, even if plaintiffs successfully argue that alter ego liability is applicable, serious limitations may remain. It is possible that under this theory only the state, and not the worker, will be able to recover.<sup>241</sup> Or, a court may find the worker to be complicit due to her status as the one who incorporated the shell corporation, and thus may see her as having unclean hands and bar her from benefiting from the discarding of that corporate entity.<sup>242</sup>

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<sup>235</sup> 18 LAURA HUNTER DIETZ ET AL., AMERICAN JURISPRUDENCE § 52 (2d ed. 2014).

<sup>236</sup> *Id.* § 63.

<sup>237</sup> See 114 NEIL A. HELFMAN, AMERICAN JURISPRUDENCE §§ 5-7 (2014).

<sup>238</sup> See 9 EMPLOYMENT COORDINATOR § 4:8 (2014) (discussing the application of alter ego liability to companies that restructure in an attempt to avoid labor laws); 70 C.J.S. *Pensions* § 98 (2014) (discussing an alter ego corporation's liability to contribute to a pension plan).

<sup>239</sup> See DIETZ ET AL., *supra* note 235, at § 63.

<sup>240</sup> *Id.*

<sup>241</sup> Marc R. Poulos, Melissa Binetti & Robert G. Reiter, Jr., *Employees or Independent Contractors? A New Test for the Construction Industry*, 96 ILL. B.J. 206, 211 (2008).

<sup>242</sup> See generally J.V.B., Annotation, *He Who Comes into Equity Must Come with Clean Hands*, 4 A.L.R. 44 (1919) (describing the unclean hands doctrine).

Although it is beyond the scope of this Article to determine the alter ego strategy's likelihood of success, or the jurisdictions in which it is most likely to be successful, at least one court has found that alter ego theory may be applicable in the independent contractor context. The case did not involve an employer's use of a worker's separate business to avoid liability, but rather the employer's use of a different shell corporation to shield itself from liability for misclassification. In *Chicago Regional Council of Carpenters v. Joseph J. Sciamanna, Inc.*, the plaintiffs sued Sciamanna, Inc. for misclassifying its workers as independent contractors.<sup>243</sup> Sciamanna, Inc. argued that it was not the proper defendant because plaintiffs' employment contracts were with an affiliated company, Sciamanna Group East, LLC.<sup>244</sup> Sciamanna, Inc. then argued that the plaintiffs failed to state a claim for alter ego liability between the two companies, and that the suit against Sciamanna Inc. should be dismissed.<sup>245</sup> The court disagreed and found the plaintiffs had sufficiently stated a claim of an alter ego relationship.<sup>246</sup> The court based this decision on allegations of the two corporations' common ownership, and that Sciamanna Inc. hired plaintiffs, paid them, and ultimately required them to sign backdated independent contractor agreements with Sciamanna Group East, LLC.<sup>247</sup> Thus, although the factual scenario is slightly different, *Sciamanna* is an example of how the theory of alter ego liability could be applied under the independent contractor misclassification framework.

### iii. Applying Other Employment Statutes When the State's Industry-Specific Statute Omits Corporations

Some states have independent contractor statutes that only apply to workers in specific industries, typically the construction industry. In states with such industry-specific statutes, there are often multiple statutes or regulations that use different standards to define independent contractors in various industries. Where an industry-specific statute explicitly states that corporations cannot be employees, plaintiffs may be able to argue that the state's general independent contractor statute should apply instead of the industry-specific statute.

In *Frahs v. Bill's Automotive, Inc.*, the court determined that under Minnesota's general independent contractor definition for unemployment, a business entity could be an employee.<sup>248</sup> After Frahs was terminated, he applied for unemployment benefits.<sup>249</sup> The Minnesota Department of Employment and Economic Development (DEED) then conducted an audit of his employer, Bill's Automotive, Inc. (BAI) and determined that Frahs was an employee of BAI.<sup>250</sup> BAI argued that Frahs was not an employee under the court's earlier decision in *Nelson v. Levy* which held that LLCs could not be employees.<sup>251</sup> Because BAI paid Frahs's wages to Frahs's company, Tom's Automotive, rather than to Frahs directly, BAI contended that Frahs's company could not be an employee under *Nelson*.<sup>252</sup> However, the court noted that the statute at issue in *Nelson* was

<sup>243</sup> No. 08 C 4636, 2009 WL 1543892, at \*1 (N.D. Ill. June 3, 2009).

<sup>244</sup> *Id.*

<sup>245</sup> *Id.*

<sup>246</sup> *Id.* at \*3-4.

<sup>247</sup> *Id.*

<sup>248</sup> No. A11-1182, 2012 WL 1593197, at \*5 (Minn. Ct. App. May 7, 2012).

<sup>249</sup> *Id.* at \*1.

<sup>250</sup> *Id.*

<sup>251</sup> *Id.* at \*5 (citing *Nelson v. Levy*, 796 N.W.2d 336, 342 (Minn. Ct. App. 2011)).

<sup>252</sup> *Id.*

inapplicable in the present case because it only applied to construction workers, and Frahs was not a construction worker.<sup>253</sup> As a result, the court looked to the applicable law, a statute that defines employment as including “services performed by ‘a member of a limited liability company who is considered an employee under the common law of employer-employee.’”<sup>254</sup> The court determined that the statute’s language did not prevent a corporation from being considered an employee and thus applied the common law factors codified in the state’s rules to ultimately find Frahs was an employee.<sup>255</sup>

Under *Frahs*’s reasoning, Minn. Stat. § 181.723 (“Section 181.723”) should have been inapplicable in the court’s decision in *Nelson* as well. In *Nelson*, the court decided that Nelson could not be considered an employee because he worked for his employer as a limited liability corporation and the LLC was not a “human being” as required by the statute.<sup>256</sup> Section 181.273 specifically states that it has limited applicability, only applying to “*individuals* performing public or private sector commercial or residential building construction or improvement services.”<sup>257</sup> Because the statute states that it applies limitedly to only individuals, and defines individuals as human beings, Nelson’s LLC fell outside the scope of the statute. Thus, Section 181.723 should be inapplicable when the worker is an LLC. This argument would be further buttressed with evidence from the legislative history, if available, that the statute was only meant to apply to individual construction workers. Even without such evidence, plaintiffs and enforcement agencies can still argue that Section 181.723 does not apply to LLCs, and Minnesota courts should instead apply Minnesota’s general unemployment compensation regulation that determines worker status for unemployment compensation to worker-LLCs.

Although this strategy may help plaintiffs in some states, it is not ideal. Typically, independent contractor statutes that target a specific industry are more protective of workers, as they are often passed to combat misclassification in industries with widespread abuse.<sup>258</sup> For example, Minnesota’s general unemployment independent contractor definition does not presume employee status, unlike Minn. Stat. § 181.723, the construction-specific statute.<sup>259</sup> Thus, a court may be more likely to find that a worker is an independent contractor under the general law than under Section 181.723, even if the worker is an employee. Plaintiffs should consider the benefits and possible risks of claiming the applicability of different statutes. A plaintiff should first argue that he falls within the scope of the more protective statute. For example, plaintiffs might first argue that Section 181.723, or a similar, more protective and specific statute, applies to business entities that are shell corporations. However, until industry-specific statutes are amended to explicitly include misclassification of workers as business entities, employers may try to avoid

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<sup>253</sup> *Id.*; see also MINN. STAT. ANN. § 181.723 subdiv. 2 (West 2014) (“This section only applies to individuals performing public or private sector commercial or residential building construction or improvement services.”).

<sup>254</sup> *Frahs*, 2012 WL 1593197, at \*5 (quoting MINN. STAT. ANN. § 268.035 subdiv. 15(a)(3) (West 2008)).

<sup>255</sup> *Frahs*, 2012 WL 1593197, at \*5; see MINN. R. 3315.0555 (2014).

<sup>256</sup> *Nelson v. Levy*, 796 N.W.2d, 336, 342-43 (Minn. Ct. App. 2011).

<sup>257</sup> MINN. STAT. ANN. § 181.723 subdiv. 2 (West 2014) (emphasis added).

<sup>258</sup> See, e.g., DONAHUE, LAMARE, & KOTLER, *supra* note 17, at 4 (noting significant rates of misclassification in the construction industry).

<sup>259</sup> Compare MINN. R. 3315.0555 (2014) (“When determining whether an individual is an employee or an independent contractor, five factors must be considered and weighed within a particular set of circumstances.”) with MINN. STAT. ANN. § 181.723 (West 2014) (presuming an individual in the construction industry is an employee unless certain conditions are met).

liability by misclassifying workers in a deliberate attempt to avoid liability under new stricter statutes. In those cases, a plaintiff may want to argue instead that a broader statute applies. At best, that argument would put workers in the same position they were in before the stricter statute was passed.

#### iv. Remedies for Workers Seeking Unemployment Benefits

If none of the above strategies apply, a worker who is trying to obtain unemployment benefits may still have a remedy. In *Rowan v. Dream It, Inc.*, the Minnesota Court of Appeals, the same court that found that construction LLCs could not be considered employees, found that Heather Rowan was eligible for unemployment benefits, despite her having contracted with Dream It, Inc. as an LLC.<sup>260</sup> When Rowan's hours as a painter for Dream It were reduced, the company convinced her to form an LLC, explaining that because her wages would be calculated in a different way, she would be able to make up the hours lost by being paid more per hour.<sup>261</sup> The company did not tell her that she would lose her employee status, her eligibility for unemployment benefits, and a guarantee of sufficient hours.<sup>262</sup> Rowan then formed her own limited liability corporation, and per Dream It's request, signed a resignation letter.<sup>263</sup> After forming the LLC and resigning, Rowan continued to perform the same services for Dream It.<sup>264</sup> Four weeks later, Dream It stopped giving Rowan assignments and Rowan applied for unemployment benefits.<sup>265</sup> Although the court followed *Nelson* in determining that an LLC could not receive unemployment benefits because it could not be an employee, it still found that Rowan was entitled to unemployment benefits.<sup>266</sup> Because Dream It convinced Rowan to form her own LLC and only informed her of the advantages, the court found that she had good cause to quit when she resigned and formed her LLC.<sup>267</sup> Thus, in this particular factual scenario, where a worker first works for the employer as an employee, and is subsequently convinced by the employer to form an LLC, the worker may be entitled to unemployment benefits. These benefits stem from workers having good cause to quit when they stop working under their own individual name, and begin working as an LLC. As a result, even if workers are unable to obtain a remedy for wage violations or workers compensation, workers may still be able to obtain unemployment benefits.

#### v. Establishing Liability for Businesses that Assist Employers in this New Misclassification

If a worker can establish that the employer is liable for misclassifying her as an independent contractor by labeling her as a franchisee, limited liability corporation, or some other corporate form, she can then try to establish liability for businesses that assist in this misclassification. For example, she can argue that companies like U&I LLC, which help employers classify workers as owners of LLCs, are liable for aiding and abetting the employer in

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<sup>260</sup> *Rowan v. Dream It, Inc.*, 812 N.W.2d 879, 880, 885 (Minn. Ct. App. 2012).

<sup>261</sup> *Id.* at 880-81.

<sup>262</sup> *Id.* at 883-84.

<sup>263</sup> *Id.* at 881.

<sup>264</sup> *Id.*

<sup>265</sup> *Id.*

<sup>266</sup> *Id.* at 882-83, 885.

<sup>267</sup> *Id.* at 885.

misclassification.<sup>268</sup> Such liability would apply regardless of how the plaintiff originally established the employer's own liability for misclassification, whether through the statute itself, alter ego liability, or a court's interpretation of an ambiguous statute.

In *Green v. Parts Distribution Xpress, Inc.*, the court found that a company that supplied independent contractor agreements to an employer could be liable for aiding and abetting the employer in violating the misclassification statute.<sup>269</sup> In so finding, the court acknowledged that the independent contractor statute that applied was silent as to the liability of third parties.<sup>270</sup> However, under common law, a party can be liable if it knows another party's conduct breaches a duty and gives this first party substantial support or encouragement in breaching the duty.<sup>271</sup> Because plaintiffs were relying on common law aiding and abetting, and because the Massachusetts statutes at issue did not preclude such liability, the court found it irrelevant that the Massachusetts statute did not expressly provide for third party liability.<sup>272</sup> The court determined the plaintiffs had successfully stated a claim for aiding and abetting liability by alleging that the defendant knew that plaintiff's employers "were planning to use the CMS form to deprive Green and others similarly situated of their rights as employees and that CMS both substantially assisted and acted in concert with PDX and Dealer Tire to accomplish that deprivation."<sup>273</sup> As a result, once the employer's liability is established, this remedy may be used to hold assisting agents liable for misclassification, even where the statute is silent as to third party liability.<sup>274</sup> However, because few cases have applied aiding and abetting liability to those who assist in misclassification, and in *Green* the court was only ruling on a motion to dismiss, it is unclear if ultimately such a remedy will be successful in individual cases or if it will be harsh enough to prevent more companies like U&I LLC from entering the market.

#### vi. Increasing Damage Awards for Workers Misclassified as Franchisees

In addition to wage remedies, which may be granted when a court finds that employees are misclassified as franchisees, plaintiffs may also be entitled to receive damages in the amount of the franchisee fees they paid to the franchisor. *Awuah v. Coverall North America, Inc. (Awuah III)* addressed the damages that *Awuah I* found were owed to plaintiff janitorial workers for their misclassification as franchisees.<sup>275</sup> The court assessed whether one janitorial worker was entitled to damages for the initial franchise fee of \$3,250 as well as monthly royalty fees and management

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<sup>268</sup> See Prichard, *supra* note 191.

<sup>269</sup> *Green v. Parts Distribution Xpress, Inc.*, No. 10-11959-DJC, 2011 WL 5928580, at \*1 (D. Mass. Nov. 29, 2011) (declining to dismiss claims against a company alleged to be aiding and abetting misclassification of workers).

<sup>270</sup> *Id.* at \*3.

<sup>271</sup> *Id.*; see also RESTATEMENT (SECOND) OF TORTS § 876 (1979) (discussing third party liability for aiding in the tortious conduct).

<sup>272</sup> *Green*, 2011 WL 5928580, at \*3.

<sup>273</sup> *Id.*

<sup>274</sup> *Id.* For a statute that expressly allows for third party liability see DEL. CODE ANN. tit. 19, § 3503(d) (West 2014) ("A person shall not knowingly incorporate or form, or assist in the incorporation or formation of, a corporation, partnership, limited liability corporation, or other entity, or pay or collect a fee for use of a foreign or domestic corporation, partnership, limited liability corporation, or other entity for the purpose of facilitating, or evading detection of, a violation of this section.") (emphasis added).

<sup>275</sup> *Awuah v. Coverall N. Am., Inc.*, 952 N.E.2d 890, 891-92 (Mass. 2011).

fees that totaled to fifteen percent of the amount Coverall charged customers.<sup>276</sup> Under the Massachusetts independent contractor statute, employees who are misclassified as independent contractors are entitled to any “damages incurred” by the misclassification.<sup>277</sup> The court found that the plaintiff was entitled to recover these franchisee fees as part of the damages incurred for misclassification.<sup>278</sup> The court reasoned that the contract for these fees violated public policy, as, in practice it “operate[d] to require employees to buy their jobs from employers” and thus was not entitled to enforcement.<sup>279</sup> As a result, workers who are misclassified as franchisees may be able to have their franchise fees returned, in addition to the other damages misclassified workers are generally are entitled to receive.

### B. Subcontracting

Some employers have used subcontracting as a way to avoid liability for misclassification. Although the presumption of employee status in the ABC test makes it more difficult for employers to do so, even the ABC test can be exploited through the use of subcontracting structures. *Jan-Pro Franchising International, Inc. v. Depianti (Jan-Pro I)* provides an example of one subcontracting business model that employers may be able to utilize to avoid liability, even if misclassification occurs. In *Jan-Pro I*, plaintiff Jan-Pro Franchising International Inc. (JPI) brought an action seeking a declaratory judgment that two of its franchisees were not its employees.<sup>280</sup> JPI created a franchise brand and franchise process, which regional franchisees paid JPI for the rights to use.<sup>281</sup> Regional franchisees subsequently entered into contracts with worker-franchisees to perform cleaning services for customers supplied by the regional franchisees.<sup>282</sup> At issue was whether the third tier worker-franchisees were employees of JPI.

In applying the Massachusetts ABC test, the court first determined that JPI met the “A” prong of the test, as JPI lacked control over the third-tier worker-franchisees; only the regional franchise at issue in the case, BradleyMktg Enterprises, Inc. (“BME”), had the ability to hire and fire the worker-franchisees and the obligation to pay them.<sup>283</sup> Additionally, JPI was not a party to the contract between the worker-franchisees and BME.<sup>284</sup> The court next determined that the worker-franchisees performed services outside the course of JPI’s business, satisfying the “B” prong of the test.<sup>285</sup> Unlike *Awuah I*, where the court rejected the franchisor’s claim that it was in the franchising business rather than the cleaning business, here, the three-tiered franchise structure helped to support JPI’s contention that it truly was in the franchise business.<sup>286</sup> JPI was not involved in running the day-to-day cleaning businesses, as it did not market cleaning services,

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<sup>276</sup> *Id.* at 894, 900-01.

<sup>277</sup> MASS. GEN. LAWS ANN. ch. 149, § 150 (West 2014).

<sup>278</sup> *Awuah*, 952 N.E.2d at 901.

<sup>279</sup> *Id.* at 900.

<sup>280</sup> *Jan-Pro Franchising Int’l, Inc. v. Depianti*, 712 S.E.2d 648, 649 (Ga. Ct. App. 2011).

<sup>281</sup> *Id.*

<sup>282</sup> *Id.* at 649-50.

<sup>283</sup> *Id.* at 651.

<sup>284</sup> *Id.*

<sup>285</sup> *Id.* at 651-52.

<sup>286</sup> *See id.* at 651.

collect payment from customers, or pay worker-franchisees for cleaning services.<sup>287</sup> The court determined that JPI merely created a business model and then sold the rights to this model.<sup>288</sup> The court then decided that the franchisees engaged in a separate business, satisfying prong “C,” for some of the same reasons the court relied upon under the previous prongs.<sup>289</sup> Because JPI was not a party to the BME and worker-franchisee contracts, exerted no control over worker-franchisees, and was engaged in the business of franchising, the franchisees were operating a distinct business.<sup>290</sup>

The court did not determine whether BME had misclassified the worker-franchisees.<sup>291</sup> However, it did mention it might have found differently if the worker-franchisees’ employee status under BME was at issue, noting that BME sends invoices to customers, collects customer payments, and sends backup franchisees to customers as needed.<sup>292</sup> Thus, where a franchisor separates itself from the worker-franchisees through another tier of franchisees, the franchisor may be able to avoid liability for misclassification, even if the franchisor’s business model defines the relationship between the middle franchisee and the worker-franchisees and leads the middle franchisee to classify workers as franchisees. As a result, even if courts find that franchisees can be considered employees, if franchisors build in enough tiers of franchisees into their model, they may be able to avoid liability, and hedge the potential solutions suggested in the previous Part.

However, where there is control between the franchisor and middle franchisee, workers and enforcement agencies may still have a remedy. In *Depianti v. Jan-Pro Franchising International, Inc. (Jan-Pro II)*, a class action was filed by the same workers at issue in *Jan-Pro I*, alleging misclassification.<sup>293</sup> The worker-franchisees this time argued that Jan-Pro was vicariously liable for BME’s misclassification of the workers because BME was acting as Jan-Pro’s agent.<sup>294</sup> Under the theory of vicarious liability, a party may be liable for another’s tortious acts based on its relationship to the tortfeasor, regardless of fault.<sup>295</sup> Thus, one possible solution for workers, whether misclassified as business entities or independent contractors, is to argue that the contractor is vicariously liable for the subcontractor’s acts, based on the master/servant relationship between the contractor and subcontractor.<sup>296</sup>

The district court certified questions to the Supreme Judicial Court of Massachusetts about the proper vicarious liability standard to apply, as a majority of courts have adopted narrower tests in the franchise context and the Massachusetts appellate court had not yet ruled on the matter.<sup>297</sup> In *Kerl v. Dennis Rasmussen, Inc.*, the court followed this majority approach to a franchisor’s vicarious liability, holding that a franchisor may only be held liable if it has control

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<sup>287</sup> *See id.*

<sup>288</sup> *Id.* at 651-52.

<sup>289</sup> *Id.* at 652.

<sup>290</sup> *Id.*

<sup>291</sup> *See id.*

<sup>292</sup> *Id.*

<sup>293</sup> *Depianti v. Jan-Pro Franchising Int’l, Inc.*, No. 08-10663-MLW, 2012 WL 3835090, at \*1 (D. Mass. Aug. 31, 2012).

<sup>294</sup> *Id.*

<sup>295</sup> *See Kerl v. Dennis Rasmussen, Inc.*, 682 N.W.2d 328, 331 (Wis. 2004).

<sup>296</sup> *See id.* at 331-32.

<sup>297</sup> *Depianti*, 2012 WL 3835090, at \*1-3.

or a right of control over the franchisee's daily operations.<sup>298</sup> The court stated that the franchise agreement itself cannot establish vicarious liability.<sup>299</sup> The court reasoned that because franchisors are frequently removed from day-to-day operations, imposing vicarious liability typically provides less deterrence for franchisors than for employers.<sup>300</sup> As a result, it would be irrelevant under this test that the JPI business model in *Jan-Pro I* and *II* defined the relationship between BME and the worker-franchisors, unless JPI was actually involved in controlling this relationship in daily operations. Where courts have adopted the majority test, it may be more challenging for franchisee plaintiffs to establish vicarious liability, and this may lead to increased classification of workers as franchisees to avoid liability. In this way, new independent contractor statutes may be pushing some employers further from the reach of the law; crafty employers who see an opportunity in the combination of franchisee classifications and subcontracting models may be able to avoid liability.

Even in this scenario, however, plaintiffs may not be completely without a remedy. Just as workers may be able to hold liable those who assist employers in business entity misclassification, even if workers cannot directly show an employee-employer relationship between themselves and the contractor, they may be able to hold the contractor liable for aiding and abetting the middle subcontractor in misclassification.<sup>301</sup> Thus, under the facts of *Jan-Pro I* and *II*, if the court were to find that BME misclassified the worker-franchisees, JPI could be held liable for aiding and abetting BME in such misclassification by creating the business model that was used to circumvent the independent contractor law. Workers' rights advocates should keep watch of this area. If this novel aiding and abetting liability fails<sup>302</sup> and enforcement of independent contractor misclassification increases, worker-franchisees may become more prevalent.

### C. Wage Avoidance

Some employers have tried to argue that the compensation their workers receive does not constitute wages, either as evidence that the worker is not an employee or to avoid or reduce the damages owed. Courts may consider payment of wages as a fact that evidences control,<sup>303</sup> as payment of wages is a factor considered in the common law right-to-control test.<sup>304</sup> Additionally, in at least one state, a worker must earn wages to be considered engaging in employment, and thus to be considered an employee.<sup>305</sup> As a result, employers may label payments to their workers as something other than wages, or have the customers pay the worker directly, and then subsequently charge the worker a fee. If successful, employers can avoid liability under the

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<sup>298</sup> *Kerl*, 682 N.W.2d at 341.

<sup>299</sup> *Id.* at 338.

<sup>300</sup> *Id.*

<sup>301</sup> *See Green*, 2011 WL 5928580, at \*3.

<sup>302</sup> *See Inomata*, *supra* note 181, at \*5 (stating that some consider *Green* as creating "new law").

<sup>303</sup> *See, e.g., Jan-Pro Franchising Int'l, Inc.*, 712 S.E.2d at 651 (finding that the fact that the workers were paid by the regional franchisees, not the franchisor, was evidence that the franchisor lacked control over worker-franchisees).

<sup>304</sup> *See Builders Commonwealth, Inc. v. Dep't of Emp't and Econ. Dev.*, 814 N.W.2d 49, 57 (Minn. Ct. App. 2012) (using mode of payment as a factor in determining employee status in applying the common law control test).

<sup>305</sup> *See, e.g., WASH. REV. CODE ANN. § 50.04.100* (West 2014) (defining "employment" as personal service performed for wages).

independent contractor statutes even if they have misclassified their employees as independent contractors.

In *Awuah v. Coverall North America, Inc.*, (*Awuah II*), the court discussed the damages owed to one plaintiff who was misclassified by Coverall as a franchisee.<sup>306</sup> In an effort to reduce its damages, the cleaning franchisor tried to argue that the money the “franchisees” received was not wages, but rather advances under an accounts receivable financing system.<sup>307</sup> Under the Coverall system, Coverall paid its workers in advance of receiving payment from customers.<sup>308</sup> However, if the customer failed to pay Coverall within ninety days, the worker was responsible for paying back the advance.<sup>309</sup> Coverall argued that because the worker at issue never worked overtime and received at least minimum wage, the worker did not incur any damages as required under the statute, and thus he was not owed any damages for the misclassification.<sup>310</sup> However, because under Massachusetts law an employer is required to pay its employees within one week of the pay period in which such wages were earned, Coverall also had to argue that payments were not actually wages, but were advances, and thus Coverall was in compliance with Massachusetts law.<sup>311</sup>

The court disagreed with Coverall and found that these advances were in fact wages, and that Coverall was trying to evade Massachusetts wage law by using this system.<sup>312</sup> The court stated that at the time the workers completed their cleaning services, they had earned their wages, and “[t]o impose an additional contingency of payment from a customer [on the worker], particularly where he had no involvement in collecting the payment, is an improper attempt to exempt Coverall from the Wage Act.”<sup>313</sup> The court ordered Coverall to pay interest on the chargebacks, as Coverall had already returned the chargebacks to the worker involved in the action.<sup>314</sup>

Because the decision involved interpretations of Massachusetts’ statutory law, the district court judge then certified questions to the Supreme Judicial Court of Massachusetts, including whether this accounts receivable financing system was proper.<sup>315</sup> In *Awuah III*, Coverall tried to argue that this account receivable financing system benefited workers and customers, enabling workers to receive payments earlier and giving them more freedom in their work.<sup>316</sup> Coverall explained that if workers are at risk of losing income when customers withhold payment, the workers have more incentive to provide adequate service, and thus require less supervision.<sup>317</sup> Without this system, Coverall claimed that it would have to increase supervision of the workers, which would impinge on the independence the workers currently possess in the workplace.<sup>318</sup>

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<sup>306</sup> *Awuah v. Coverall N. Am., Inc.*, 740 F. Supp. 2d 240, 243-45 (D. Mass. 2010).

<sup>307</sup> *Id.* at 244.

<sup>308</sup> *Id.*

<sup>309</sup> *Id.*

<sup>310</sup> *Id.* at 242.

<sup>311</sup> *Id.* at 243-44.

<sup>312</sup> *Id.* at 244-45.

<sup>313</sup> *Id.* at 245.

<sup>314</sup> *Id.*

<sup>315</sup> *Id.* at 245; *Awuah*, 952 N.E.2d at 893.

<sup>316</sup> *Awuah*, 952 N.E.2d at 896.

<sup>317</sup> *Id.*

<sup>318</sup> *Id.*

Ultimately, the court agreed with the district court and held that the classification of wages as advances violates the Massachusetts Wage Act.<sup>319</sup> The court rejected Coverall's arguments, stating that Coverall could impose sanctions or terminate a worker with poor work performance, but Coverall could not withhold a worker's wages as either a sanction or performance incentive.<sup>320</sup> Thus, although employers have attempted to avoid both liability and damages by changing how they label the worker and the worker's wages, in both contexts, courts appear to be looking beyond the employer's label.<sup>321</sup>

In some states, by labeling income as something other than wages, employers can actually prevent a worker's claim from even being considered. In Washington, the same issue raised in *Awuah* has surfaced. However, because the Washington unemployment insurance statute is structured differently, the issue arises before the determination of damages. Although Washington has instituted a presumptive ABC test to define independent contractors,<sup>322</sup> first a worker must prove that he is engaging in employment, which requires showing that he is performing personal services for wages.<sup>323</sup> Thus, if a court determines that a worker was not paid wages, the claim will not proceed. In *Kabrick v. Employment Security Department of the State of Washington*, the Court of Appeals of Washington upheld the Employment Security Department's denial of unemployment benefits to Barbara Kabrick for this very reason.<sup>324</sup> The court found that as a taxi driver for Spo-Cab Inc., Ms. Kabrick did not earn wages because the money she was paid by customers did not belong to Spo-Cab.<sup>325</sup> If Ms. Kabrick was paid in cash, she kept the entire fare, and if a customer paid by credit card, Spo-Cab would return almost the entire fare to her, except for a small handling fee.<sup>326</sup> Consequently, the court found that Spo-Cab merely "facilitated their collection of fares" rather than paid wages, and as a result, Ms. Kabrick was not engaging in employment for Spo-Cab.<sup>327</sup>

These threshold questions heavily increase the burden on workers, a result contrary to the intention of the presumptive employee statute. Moreover, the wage inquiry may actually have little to do with whether one is in reality an independent contractor. As such, including wages as a threshold factor not only increases the burden on workers, but also significantly heightens the importance of a factor that may be irrelevant. For example, in the Washington court's consideration of what constitutes wages, the court defines the wage test as whether the money ever belonged to the employer.<sup>328</sup> This test leaves room for crafty employers to evade the law

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<sup>319</sup> *Id.* at 893, 896-97, 901.

<sup>320</sup> *Id.* at 897.

<sup>321</sup> See also *Builders Commonwealth, Inc.*, 814 N.W.2d at 58 (finding employer's labeling of payments as "advances" or "loans" was not controlling and that such "advances" were wages under Minnesota unemployment insurance law).

<sup>322</sup> See WASH. REV. CODE ANN. § 50.04.140 (West 2014).

<sup>323</sup> See WASH. REV. CODE ANN. § 50.04.100 (West 2014) ("'Employment,' subject only to the other provisions of this title, means personal service, of whatever nature, unlimited by the relationship of master and servant as known to the common law or any other legal relationship, including service in interstate commerce, performed for wages or under any contract calling for the performance of personal services, written or oral, express or implied.").

<sup>324</sup> *Kabrick v. Emp't Sec. Dep't of Wash.*, No. 20126-1-III, 2002 WL 91270, at \*6 (Wash. Ct. App. Jan. 24, 2002).

<sup>325</sup> *Id.*

<sup>326</sup> *Id.*

<sup>327</sup> *Id.*

<sup>328</sup> *Id.*

merely by changing the order in which workers are paid and the party from whom the employer receives payment. For instance, although Ms. Kabrick was able to keep almost the entire fare paid by customers, she ultimately gave some of this money back to Spo-Cab.<sup>329</sup> As part of her agreement with Spo-Cab, she paid Spo-Cab a dispatch fee and administration fee on a weekly basis.<sup>330</sup> The dispatch fee was based on working sixty hours per week, and was not adjusted if a driver worked less.<sup>331</sup> Whether a worker is paid directly by customers, and later gives a share to his or her employer, or whether the customer pays the employer first, should have little to do with whether one is an employee or an independent contractor.

At the very least, whether a worker is paid wages is of no greater significance than any other fact that goes into the independent contractor analysis. Thus, it should only be considered in analyzing whether an employer exerts control over the worker, the “A” prong of the ABC test, or in reference to any of the other prongs of the test if relevant. Under this approach, all facts can be analyzed and weighed together, at the same time, to determine if the totality of these facts suggests an employee or an independent contractor relationship.

In *Kabrick*, many facts suggested that the worker was an employee under Washington’s presumptive ABC test. For example, Spo-cab trained its drivers, controlled their schedules, prohibited them from working for other companies or hiring substitutes, and fined them for late paperwork and unclean cabs.<sup>332</sup> As a result, if the court was able to engage in the actual independent contractor analysis it may have found differently. As it stands, Washington’s threshold analysis can be used as a mechanism to prevent the court from reaching the actual independent contractor analysis, where it can evaluate all of the facts at the same time. Instead, it forces the court to first focus separately on smaller factors that can be easily manipulated.

The Washington statute should be altered to remove this threshold inquiry. Until that occurs, plaintiffs can argue that employers are merely trying to circumvent the law through such reordering of payments. Plaintiffs can rely on *Awuah II* and *Awuah III* as examples of a court rejecting such relabeling of wages, arguing that reordering allows employers to circumvent the independent contractor misclassification statute. If successful, and the court ultimately finds the workers to be employees, plaintiffs can also argue based on *Awuah III* that this payment system violates public policy, as it forces employees to pay for their jobs.<sup>333</sup> The employer would then be required to refund the fees charged, such as the dispatch and administration fees in *Kabrick*.

#### *D. Use of Semantic Distinctions to Allege Lack of Control and Different Courses of Business*

With new presumptive and conjunctive independent contractor tests, many employers have tried to re-characterize their employment relationships, incorporating language from independent contractor statutes into their independent contractor agreements with their workers. First, this Part will briefly explore this phenomenon and courts’ reactions. This Part will then address unsuccessful employer attempts to re-characterize the nature of their business to get around the “B” prong in the ABC test that requires an independent contractor to perform services

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<sup>329</sup> *Id.*

<sup>330</sup> *Id.* at \*1.

<sup>331</sup> *Id.* at \*2.

<sup>332</sup> *Id.*

<sup>333</sup> See *Awuah*, 952 N.E.2d at 900-901.

outside the usual course of business of the employer.<sup>334</sup> Although there are myriad factual circumstances in independent contractor cases, there are common arguments employers have made in an attempt to prove the worker does not meet this element.

### 1. Contract Drafting

Under the presumptive ABC test, generally, employers must prove three elements: the worker is free from control, the worker performs services outside the employer's course of business, and the worker has his or her own independent business that typically performs the same services as those done for the employer.<sup>335</sup> Some employers have included language from this test in their independent contractor agreements. Employers that correctly classify workers as independent contractors may also include such language in their independent contractor agreements when it reflects the reality of the relationship. However, employers attempting to evade independent contractor laws may use the independent contractor agreement as evidence that the worker is an independent contractor, even if the arrangement in practice functions differently than the employer's carefully selected language suggests. For example, some employers have specifically written into their contracts that the worker has sole control over his or her work, when the employer in practice controlled its workers.<sup>336</sup> In *Western Ports*, the court looked beyond the wording of the contract, finding that the worker was not in reality free from the employer's control.<sup>337</sup> In making this determination, the court found it significant that the worker, a truck driver, was required to clean his truck, obtain company permission to carry passengers, and go to the company dispatch center to receive new unscheduled assignments.<sup>338</sup> Additionally, truck drivers could be disciplined or terminated for violating any company policy, and more specifically, for tardiness, dishonesty, theft, unsafely operating the truck, as well as a number of other acts.<sup>339</sup> Other courts have similarly found that the independent contractor agreement is not dispositive, and have engaged in an analysis of the actual control exerted by the employers.<sup>340</sup> As a result, although employers will likely continue to tailor their independent contractor agreements in a way that looks as though the worker meets the elements, thus far it has had little impact on courts' ultimate evaluation. In this regard, once again, courts have chosen to look beyond mere labels. To ensure that courts continue to look beyond labels, it may be important for states to explicitly include in the "A" prong that the worker's freedom from control must be found both in the contract and in fact, as has been done by Massachusetts, Maryland, New York and

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<sup>334</sup> See, e.g., MASS. GEN. LAWS ANN. ch. 149, § 148B(a)(2) (West 2014).

<sup>335</sup> See, e.g., WASH. REV. CODE ANN. § 50.04.140(1) (West 2014); N.J. STAT. ANN. § 34:20-4 (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-903(c)(1)(ii) (LexisNexis 2014).

<sup>336</sup> See, e.g., *W. Ports Transp., Inc. v. Emp't Sec. Dep't of Wash.*, 41 P.3d 510, 514 (Wash. Ct. App. 2002) (quoting contractual language that "the manner and means of conducting the work are under the sole control of the Contractor"); *Kabrick*, No. 20126-1-III, 2002 WL 91270, at \*1 (quoting language from the Dispatch Agreement that the driver is "free from interference or control on the part of Spokane Cab in the operation of said taxicab").

<sup>337</sup> *W. Ports Transp., Inc.*, 41 P.3d at 516 ("Contractual language, such as a provision describing drivers as independent contractors, is not dispositive; instead, the court considers all the facts related to the work situation."); *id.* at 520.

<sup>338</sup> *Id.* at 517-18.

<sup>339</sup> *Id.* at 518.

<sup>340</sup> See, e.g., *Penick v. Emp't Sec. Dep't*, 917 P.2d 136, 142-43 (Wash. Ct. App. 1996) ("[C]ontracts alone are not dispositive.").

Nebraska.<sup>341</sup>

## 2. “Course of Business” Semantic Arguments

In Massachusetts, a number of employers have tried to re-characterize the purpose of their businesses to argue that their workers are engaged in services distinct from services the business provides. This argument is especially important in states like Massachusetts where an employer can only argue that the workers work outside the usual course of the employer’s business to meet the “B” prong of their ABC test.<sup>342</sup> Under some other states’ ABC statutes, employers have the option of proving the workers work outside of the employer’s place of business instead.<sup>343</sup> However, no matter which form of the statute the state uses, these arguments still have an impact where the worker does work in the employer’s usual place of business.

In three separate cases in which exotic dancers for different employers claimed they were misclassified, the employers tried to argue that they were not in the business of providing exotic dancing, but rather that the employers were in the business of selling alcohol.<sup>344</sup> In the first case that arose, employer King Arthur’s Lounge analogized its business to a sports bar and its workers to televisions in that sports bar.<sup>345</sup> It explained that dancing is simply a form of entertainment provided for customers, just as televisions and pool tables in sports bars provide entertainment to customers.<sup>346</sup> King Arthur’s argued that just as a sports bar’s provision of televisions and pool tables does not mean that the sports bar is in the business of sports, King Arthur’s provision of exotic dancers did not mean that it was in the business of providing exotic dancing.<sup>347</sup> In rejecting this argument, the court stated that it “would need to be blind to human instinct to decide that live nude entertainment was equivalent to the wallpaper of routinely-televised matches, games, tournaments and sports talk in such a place.”<sup>348</sup> The court explained that customers attend exotic dancing establishments to see exotic dancers, whereas patrons at sports bars attend mainly to purchase alcohol; watching television and playing pool are secondary.<sup>349</sup> Additionally, the stage

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<sup>341</sup> MASS. GEN. LAWS ANN. ch. 149, § 148B(a)(1) (West 2014); MD. CODE ANN., LAB. & EMPL. § 3-903(c)(1)(ii)(1) (LexisNexis 2014); N.Y. LAB. § 861-c(1)(a) (McKinney 2014); NEB. REV. STAT. ANN. § 48-604(5)(a) (LexisNexis 2014).

<sup>342</sup> See MASS. GEN. LAWS ANN. ch. 149, § 148B(a)(2) (West 2014) (“[T]he service is performed outside the usual course of the business of the employer . . .”).

<sup>343</sup> See, e.g., WASH. REV. CODE ANN. § 50.04.140(1)(b) (West 2014) (“Such service is either outside the usual course of business for which such service is performed, or that such service is performed outside of all the places of business of the enterprises for which such service is performed . . .”); N.J. STAT. ANN. § 34:20-4(b) (West 2014) (“[T]he service is either outside the usual course of the business for which the service is performed, or the service is performed outside of all the places of business of the employer for which the service is performed . . .”); MD. CODE ANN., LAB. & EMPL. § 3-903(c)(1)(ii)(3) (LexisNexis 2014) (“[T]he work is[(A)] outside of the usual course of business of the person for whom the work is performed; or [(B)] performed outside of any place of business of the person for whom the work is performed.”).

<sup>344</sup> *Chaves v. King Arthur’s Lounge, Inc.*, No. 07-2505, 2009 WL 3188948, at \*1 (Mass. Super. July 30, 2009); *Monteiro v. PJD Entm’t of Worcester, Inc.*, No. 101930, 2011 WL 7090703, at \*1 (Mass. Super. Nov. 23, 2011); *Jenks v. D. & B. Corp.*, No. 09-01978, 2011 WL 3930190, at \*3 (Mass. Super. Aug. 24, 2011).

<sup>345</sup> *Chaves*, 2009 WL 3188948, at \*1.

<sup>346</sup> *Id.*

<sup>347</sup> *Id.*

<sup>348</sup> *Id.*

<sup>349</sup> *Id.*

the dancers performed upon was in the center of the lounge, unlike sports bars, which have no special architectural design that allows patrons to better view televisions.<sup>350</sup> Ultimately, the court found that King Arthur's was in the business of providing adult entertainment, and that the dancers work in the course of that business because of the revenue derived from exotic dancing services and its overall importance to this business.<sup>351</sup>

Similarly, in *Monteiro v. PJD Entertainment of Worcester, Inc.*, employer Centerfolds argued that it was in the restaurant and bar business, and merely allowed exotic dancers to perform.<sup>352</sup> The court rejected this argument, ruling broadly that a business that serves alcohol and that has a place for exotic dancers to perform is in the adult entertainment business.<sup>353</sup> As a result, the court found that the plaintiff exotic dancers had been misclassified because their dancing was in the course of Centerfold's adult entertainment business.<sup>354</sup> Thus, in the exotic dancing context, courts have so far rejected employers' attempts to argue that a specific part of the business is the entirety of the business and that the service the workers at issue perform is not the business's focus.

These arguments are not unique to the employment of exotic dancers. In *Awuah I*, the defendant franchisor argued that the janitorial franchisee plaintiffs were not performing services in the course of its business by claiming that it was not in the cleaning business, but rather in the franchise business.<sup>355</sup> Similarly, in *Network Communications, Inc. v. Employment Security Department of the State of Washington*, the court determined that newspaper deliverers worked in the course of the employer's business, despite the employer's attempt to argue that it was in the business of publishing newspapers, rather than delivering newspapers.<sup>356</sup> The court found that Network Communications was in the business of both publishing and delivering papers.<sup>357</sup> Thus, despite some employers' attempts to re-characterize the nature of their businesses, courts have been unwilling to draw such stringent lines in defining a business's purpose and have rejected an employer's attempt to limit and distinguish its business from the services that many of its workers perform.

In another case involving newspaper deliverers, the court similarly found that the employer was in the business of both publishing and delivering papers.<sup>358</sup> However, the statute at issue was the Massachusetts unemployment insurance statute, which uses the version of the ABC test that allows employers to prove either that the worker performed services outside the usual course of the employer's business, *or* worked outside the employer's place of business.<sup>359</sup> Because such newspaper deliverers delivered papers outside of the Athol Daily News building, the court found that the workers did not perform services in Athol Daily News's place of

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<sup>350</sup> *Id.*

<sup>351</sup> *Id.*

<sup>352</sup> *Monteiro*, 2011 WL 7090703, at \*2.

<sup>353</sup> *Id.*

<sup>354</sup> *Id.*; *see also Jenks*, 2011 WL 3930190, at \*3-4 (finding plaintiff exotic dancers were misclassified as independent contractors because plaintiffs performed services in the course of Golden Banana's adult entertainment business).

<sup>355</sup> *Awuah v. Coverall N. Am., Inc.*, 707 F. Supp. 2d 80, 82-83 (D. Mass. 2010).

<sup>356</sup> *Network Comm'n, Inc. v. Emp't Sec. Dep't of Wash.*, No. 60212-8-I, 2008 WL 1851103, at \*4 (Wash. Ct. App. Apr. 28, 2008).

<sup>357</sup> *See id.*

<sup>358</sup> *Athol Daily News v. Bd. of Review of Div. of Emp't and Training*, 786 N.E.2d 365, 372 (Mass. 2003).

<sup>359</sup> *See id.* at 369-370 (referencing ABC test in MASS. GEN. LAWS ANN. ch. 151A, § 2).

business.<sup>360</sup> Thus, some versions of the ABC test can still be strengthened by eliminating the place of business portion of this prong of the test. To prove a worker is an independent contractor, even with the place of business portion present, the employer still has to prove the worker is outside of its control and engaged in an independent business. However, this version of the test places too much weight on the innocuous factor of where a worker performs its services. Although where the worker works might be relevant to the analysis, it is likely a factor that may influence the course of business determination or the control element, and thus is not so dispositive that it should be explicit in the test.

#### IV. CONCLUSION

States have taken action against misclassification, and it appears their actions in many cases have followed the most effective statutory models available. While strategies have been tailored to the existing laws of each state as well as to varied political realities, the three-pronged ABC test and the presumption of employee status have clearly taken hold as the favored model for defining an independent contractor. Revising statutes towards this test is a particularly effective measure when it creates a set of laws that provide one independent contracting definition across all workers, although there are valid arguments in favor of tackling legislative reform aimed at certain industries. While states have undertaken understandable alterations to ABC, in some cases including additional objective criteria that could narrow the ability of courts to infuse the application of ABC with common law interpretation, such variety across states blocks the expansion of a uniform standard for independent contracting across the country.

Measuring the particular efficacy of changes to the penalization of misclassification and the enforcement of such laws is more challenging. Nonetheless, states appear to be vigorously experimenting with mechanisms to increase compliance with their laws, including the penalization of intentional misclassification, the use of criminal liability and stop-work orders, and the implementation of successor liability and private rights of action. Given the costs when state agencies carry the burden of investigating misclassification, this menu of strategies should be adopted together rather than as alternatives to each other. Changes to simplify and clarify independent contracting definitions benefit well-intentioned employers, while increased punishments can be aimed at employers who endeavor to break the law. Moreover, such penalties can serve to invest the law-abiding business community in the state's effort to crack down on misclassification. States should communicate about the usefulness of new measures, as a standard set of punishments across states could assist in placing employers on notice of the stakes of misclassification.

While the wave of legislation across states amending or instituting new independent contractor laws has made it more difficult for employers to misclassify workers, some employers have still found new ways to avoid liability under these statutes. Yet, not every new tactic has been successful. Our preliminary analysis suggests that the ABC test is fair to both workers and employers, although some improvements are still needed. Repeatedly, employers have attempted to use labels or semantic distinctions to avoid liability under these statutes. To establish that they lack control over their workers, under the "A" prong of the ABC test, employers have phrased their independent contractor agreements to reflect a lack of control. Other employers have argued that their workers are not paid wages, as evidence that this control is lacking or that there is simply no employment relationship at all. Employers have also used semantic distinctions to

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<sup>360</sup> *Id.*

argue that workers perform services outside of the employers' course of business; the "B" prong of the ABC test. Employers have tried to distinguish services performed by workers from the main purpose of the business. On the whole, most courts have rejected such hollow distinctions.

In Utah, Minnesota, Washington and Massachusetts, employers have contracted with workers as business entities, such as LLCs or franchisees, in an attempt to avoid both the wage and tax obligations that come with hiring employees, as well as the increasing likelihood of being found liable for misclassification under presumptive statutes.<sup>361</sup> Faced with these new classifications, some courts have still engaged in the independent contractor analysis, using the "B" and "C" prongs as guides to determine whether such entities are in fact distinct businesses, separate from the employer's business. In other states, employers have been successful at using this new form of misclassification to avoid liability for independent contractor misclassification because the statute prevents corporate forms from being employees. Statutory schemes need to be corrected to close this loophole, applying the employee presumption to all business entities. Even if statutes are amended, however, some employers may still be able to avoid liability for misclassification through the use of subcontracting. Even if a second tier contractor misclassifies workers according to the contractor's plan, if the contractor does not have a direct relationship to the workers, the contractor may be able to avoid liability. Worker plaintiffs can argue that the employer is vicariously liable for the second tier's misclassification, and depending on the law in the jurisdiction, they may be successful. As enforcement actions increase, workers' rights advocates should monitor these areas of concern, and advocate for statutory reform where it is still needed, to prevent the problems identified from becoming more widespread.

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<sup>361</sup> See UTAH CODE ANN. § 34A-2-103 (LexisNexis 2014); MINN. STAT. ANN. § 181.723 (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014); WASH. REV. CODE ANN. § 50.04.140 (West 2014).

## APPENDIX

State	Statutes Cited
California	CAL. LAB. CODE § 226.8 (West 2014)
Colorado	COLO. REV. STAT. § 8-72-114 (2014)
Connecticut	CONN. GEN. STAT. ANN. § 31-69 (West 2014); CONN. GEN. STAT. ANN. § 31-69a (West 2014); CONN. GEN. STAT. ANN. § 31-76a (West 2014); CONN. GEN. STAT. ANN. § 31-288 (West 2014)
Delaware	DEL. CODE ANN. tit. 19, § 3501 (West 2014); DEL. CODE ANN. tit. 19, § 3502 (West 2014); DEL. CODE ANN. tit. 19, § 3503 (West 2014); DEL. CODE ANN. tit. 19, § 3505 (West 2014); DEL. CODE ANN. tit. 19, § 3507 (West 2014); DEL. CODE ANN. tit. 19, § 3508 (West 2014); DEL. CODE ANN. tit. 19, § 3509 (West 2014)
Illinois	820 ILL. COMP. STAT. ANN. 185/10 (West 2014); 820 ILL. COMP. STAT. ANN. 185/25 (West 2014); 820 ILL. COMP. STAT. ANN. 185/40 (West 2014); 820 ILL. COMP. STAT. ANN. 185/45 (West 2014); 820 ILL. COMP. STAT. ANN. 185/50 (West 2014); 820 ILL. COMP. STAT. ANN. 185/55 (West 2014); 820 ILL. COMP. STAT. ANN. 185/60 (West 2014); 820 ILL. COMP. STAT. ANN. 185/75 (West 2014)
Indiana	IND. CODE ANN. § 6-8.1-3-21.2 (West 2014); IND. CODE ANN. § 22-2-15-2 (West 2014)
Kansas	KAN. STAT. ANN. § 44-703 (West 2014); KAN. STAT. ANN. § 44-719 (West 2014)
Maine	ME. REV. STAT. ANN. tit. 26, § 1043 (2014); ME. REV. STAT. ANN. tit. 39-A, § 102 (2014); ME. REV. STAT. ANN. tit. 39-A, § 102(13) (2010) (repealed 2011); ME. REV. STAT. ANN. tit. 39-A, § 105-A (2014); ME. REV. STAT. ANN. tit. 39-A, § 105-A (2014)
Maryland	MD. CODE ANN., LAB. & EMPL. § 3-902 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-903 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-903.1 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-908 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-909 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-911 (LexisNexis 2014); MD. CODE ANN., LAB. & EMPL. § 3-915 (LexisNexis 2014)
Massachusetts	MASS. GEN. LAWS ANN. ch. 149, § 27C (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 148B (West 2014); MASS. GEN. LAWS ANN. ch. 149, § 150 (West 2014)
Minnesota	MINN. STAT. ANN. § 181.722 (West 2014); MINN. STAT. ANN. § 181.723 subdiv. 4 (West 2011) (amended 2012); MINN. STAT. ANN. § 326B.701 (West 2014); MINN. R. 3315.0555 (2014)

Nebraska	NEB. REV. STAT. ANN. § 48-604 (LexisNexis 2014); NEB. REV. STAT. ANN. § 48-2903 (LexisNexis 2014); NEB. REV. STAT. ANN. § 48-2907 (LexisNexis 2014)
New Hampshire	N.H. REV. STAT. ANN. § 275:4 (2014)
New Jersey	N.J. STAT. ANN. §34:20-1 (West 2014); N.J. STAT. ANN. § 34:20-4 (West 2014); N.J. STAT. ANN. § 34:20-5 (West 2014); N.J. STAT. ANN. § 34:20-8 (West 2014)
New Mexico	N.M. STAT. ANN. § 60-13-3.1 (West 2005)
New York	N.Y. LAB. LAW § 861-c (McKinney 2014); N.Y. LAB. LAW § 861-e (McKinney 2014); N.Y. LAB. LAW § 861-f (McKinney 2014)
Oregon	OR. REV. STAT. ANN. § 670.600 (West 2014); OR. REV. STAT. ANN. § 670.700 (West 2014)
Pennsylvania	43 PA. STAT. ANN. § 933.3 (West 2014); 43 PA. STAT. ANN. § 933.5 (West 2014); 43 PA. STAT. ANN. § 933.6 (West 2014); 43 PA. STAT. ANN. § 933.7 (West 2014)
Utah	UTAH CODE ANN. § 34-28-2 (LexisNexis 2014); UTAH CODE ANN. § 34A-2-103 (LexisNexis 2014); UTAH CODE ANN. § 34A-2-110 (LexisNexis 2014); UTAH CODE ANN. § 58-55-301 (LexisNexis 2014)
Vermont	VT. STAT. ANN. tit. 21, § 692 (West 2014); VT. STAT. ANN. tit. 21, § 708 (West 2014); VT. STAT. ANN. tit. 21, § 710 (West 2014); VT. STAT. ANN. tit. 21, § 1314a (West 2014)
Washington	WASH. REV. CODE ANN. § 49.44.170 (West 2014); WASH. REV. CODE ANN. § 50.04.100 (West 2014); WASH. REV. CODE ANN. § 50.04.140 (West 2014); WASH. REV. CODE ANN. § 50.04.145 (West 2014); WASH. REV. CODE ANN. § 51.08.181 (West 2014); WASH. REV. CODE ANN. §51.08.195 (West 2014)
Wisconsin	WISC. STAT. ANN. § 103.005 (West 2014); WISC. STAT. ANN. § 103.06 (West 2014)