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WASHINGTON, DC

MEMORANDUM

TO: PCA

FROM: Russell A. Hollrah

DATE: August 14 ,2015

RE: August Legislative Update

The following discusses two important legislative developments that should be of interest to PCA members. The first concerns a bill recently introduced in the U.S. Congress that would affect firms that do business with independent contractors, and the other discusses recently enacted state legislation affecting independent-contractor status.

I. Payroll Fraud Prevention Act of 2015 Re-Introduced

The *Payroll Fraud Prevention Act of 2015*, introduced on July 29, 2015, by Senator Bob Casey (D-Pa), would (i) impose new administrative burdens on firms that do business with certain independent-contractor service providers, and (ii) expose such firms to draconian civil penalties if any of those service providers were determined not to qualify as independent contractors for purposes of the Fair Labor Standards Act ("FLSA").

Initial cosponsors of the bill, S. 1896, are Senators Al Franken (DFL-Minn), Patty Murray (D-Wash), Elizabeth Warren (D-Mass), Sherrod Brown (D-Ohio), and Jeff Merkley (D-Ore). This bill is substantially the same as prior versions of the *Payroll Fraud Prevention Act* that were introduced in 2013 by Senator Casey, S. 1687, and in 2011 by Senator Brown, S. 770.

A companion bill, H.R. 3427, was introduced in the House of Representatives on the same day by Representative Frederica Wilson (D-Fla). Initial cosponsors of this bill are Representatives Bobby Scott (D-Va), John Conyers (D-Mich) and Donald Payne (D-NJ). A prior version of this bill was introduced in 2014 as H.R. 4611 by Representative Joe Courtney (D-CT).

While the prospects for the *Payroll Fraud Prevention Act of 2015* in the current Congress are not positive, the re-introduction of this bill – for the third time – signifies the unrelenting

commitment of its sponsors to increase the financial risks to firms that choose to do business with independent contractors and thereby impede the ability of self-employed individuals to operate their businesses. The new financial risks to which this bill would expose potential clients of self-employed individuals would create a powerful financial incentive for such potential clients to eschew independent contractors and instead do business with larger entities.

S. 1896 would create two new categories of individuals under the FLSA, called "non-employees" and "covered individuals."

A "non-employee" would be defined as an individual who is not an employee of a person but is engaged by the person to perform services within the course of the person's trade or business.

A "covered individual" would be defined as an individual who is either:

(i) an employee of a person, or
(ii) a nonemployee of a person (including an individual who is an employer), provided that the person engages the individual to perform services within the course of the trade or business of the person and
    a. the person is required to issue an Internal Revenue Service Form 1099 to the individual, or
    b. the person would be so required were it not for the fact that the individual operates through a legal entity, such as a corporation or LLC, provided that
        i. the individual has an ownership interest in the entity of any amount, and
        ii. the person requires the individual to operate out of such an entity as a condition of doing business.

The bill would require a firm that hires an employee or engages a "non-employee" engaged in commerce or in the production of goods for commerce to:

- Properly classify each "covered individual" as an employee or a non-employee; and
- Provide each "covered individual" with a specified written notice informing the individual that the individual is being classified as an employee or a "non-employee" and containing other specified information concerning the U.S. Department of Labor and the consequences to an individual of being classified as an independent contractor.

The notice would need to be provided within six months after the date of enactment to existing "covered individuals" and upon the commencement of services by new "covered individuals" or upon a change in status.

If a person fails to timely comply with the new notice requirement, the individual would be presumed to be an employee of the person for purposes of the FLSA, which presumption could be rebutted only by satisfying the demanding "clear and convincing evidence" standard.

The bill would expand the FLSA's anti-retaliation protections by including within its list of prohibited acts a person discharging, or taking any other discriminatory action against, a "covered individual" who engages in any conduct opposing or contesting the person's

classification of a "covered individual" as an employee or a "non-employee" for purposes of the FLSA or federal employment taxes.

The misclassification of a "covered individual" as a non-employee for purposes of the FLSA would become a stand-alone FLSA violation under S. 1896. The liquidated damages otherwise recoverable for FLSA violations would be doubled with respect to "covered individuals" when the violation was caused by the misclassification of the "covered individual." This doubling of the liquidated damages would create a potential liability of triple the amount of unpaid wages found to be owed.

The bill also would expand the civil penalties that DOL can impose for FLSA violations by imposing a per-individual civil penalty of up to $1,100 ($5,000 in a case of repeated or willful violations) for any violation of the FLSA's (i) minimum wage requirement; (ii) overtime requirement; (iii) recordkeeping requirement; (iv) duty to correctly classify "covered individuals" as employees or independent contractors; or (v) new notice requirement for "covered individuals." These proposed penalties would apply not only in a case where a "covered individual" is misclassified, but also in a case where a specified FLSA violation occurs with respect to any individual, including an individual whom the person treats as an employee for purposes of the FLSA.

The DOL would be required to create a new "employee rights" website summarizing the rights of employees and non-employees under the FLSA.

The bill would impose new requirements for states to intensify their auditing of companies in search of misclassified workers for purposes of state unemployment taxes. It also would require the DOL to institute internal practices to share information of worker misclassification with its Wage and Hour division and to target for auditing those industries with a frequent incidence of worker misclassification, as determined by the Secretary of DOL. Types of businesses that DOL has recently targeted include janitorial, construction, home care, transportation/trucking, cable installation, landscaping, and car/limousine services.

Comments:

The *Payroll Fraud Prevention Act of 2015* would impose draconian financial sanctions on firms that misclassify certain individuals as independent contractors, and thereby significantly increase the financial risks of doing business with self-employed individuals.

S. 1896 would bring heightened significance to whether the type of services a person engages an independent contractor to perform are "within the course of the person's trade or business," as such individuals can qualify as a "covered individual." The significance of "covered individual" status is that such individuals would be covered by the proposed new notice requirements, anti-retaliation protections, "triple damages," and civil penalties for misclassification.

While current law imposes a civil penalty of up to $1,100 only with respect to a specified FLSA violation that is found to be *repeated* or *willful*, the bill would require such a finding only with respect to the higher-tier civil penalty of up to $5,000. A specified FLSA

violation is all that would be required under the bill to subject an employer to the lower-tier civil penalty of up to $1,100 per individual.

II. Four States Enact Laws Affecting the Definition of "Independent Contractor"

Arkansas, Indiana, Nevada, and South Dakota enacted legislation this year affecting the determination of whether a worker is an employee or independent contractor for certain purposes. Several of the new laws are relevant to caregiver registries, while others are not. All are included to provide a sense of the overall direction in which the recently enacted legislation affecting independent-contractor status appears to be moving. On balance, the changes are supportive of independent-contractor status. The specific provisions are discussed below.

A. Arkansas

Arkansas enacted two new laws, namely, one modifying the state's "ABC" test and the other concerning the "sharing economy."

H.B. 1540 modified the state's "ABC" test for determining whether a worker is an independent contractor for unemployment purposes. The new law provides that effective April 2, 2015, an independent-contractor relationship is established if the relationship satisfies factors A and *either* B or C. The prior version of the test was met only if all three factors, namely, A and B and C, were satisfied. The effect of this change is to expand the definition of independent contractor for purposes of unemployment.

The amended "ABC" test provides:

> (e) Service performed by an individual for wages shall be deemed to be employment subject to this chapter irrespective of whether the common law relationship of master and servant exists, unless and until it is shown to the satisfaction of the director that:
>
> (1) The individual has been and will continue to be free from control and direction in connection with the performance of the service, both under his or her contract for the performance of service and in fact; *and*
>
> (2)(A) The service is performed either outside the usual course of the business for which the service is performed or is performed outside all the places of business of the enterprise for which the service is performed; *or*
>
> (B) 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.

Representative Robin Lundstrum (R) introduced H.B. 1540 on March 2, 2015, and Governor Asa Hutchinson (R) signed it into law on April 2, 2015.

In addition, Arkansas enacted S.B. 800, which deems certain transportation network company ("TNC") drivers to be statutory independent contractors for workers' compensation purposes. The common law test is otherwise used to determine an individual's status for these purposes.

The new provisions, which are contained in the state's Motor Vehicle law, define a TNC to mean "an individual or entity licensed under this subchapter that operates in this state and uses a website, digital network, or software application to connect passengers to transportation network company services provided by transportation network company drivers." Uber and Lyft likely could qualify as TNCs if they are licensed.

S.B. 800 deems TNC drivers to be independent contractors relative to a TNC if the following five factors are satisfied:

> (1) The transportation network company does not prescribe specific hours during which a transportation network company driver must be logged into the transportation network company's website, digital platform, or software application;
>
> (2) The transportation network company imposes no restrictions on the transportation network company driver's ability to utilize a website, digital network, or software application of other transportation network companies;
>
> (3) The transportation network company does not assign a transportation network company driver a particular territory in which transportation network company services may be provided;
>
> (4) The transportation network company does not restrict a transportation network company driver from engaging in any other occupation or business; and
>
> (5) The transportation network company and transportation network company driver agree in writing that the transportation network company driver is an independent contractor of the transportation network company.

Senator Jason Rapert (R) introduced S.B. 800 on March 4, 2015, and on April 4, 2015, Governor Hutchinson signed it into law.

B. Indiana

Indiana created a comprehensive regulatory scheme governing TNCs. The new law, enacted as H.B. 1278, also provides that effective July 1, 2015:

> Except as otherwise provided in a written contract:

> (1) a TNC driver who connects to a TNC's digital network is an independent contractor of the TNC; and
>
> (2) a TNC is not considered to do either of the following:
>
> (A) Control, direct, or manage a TNC driver who connects to the TNC's digital network.
>
> (B) Own, control, operate, or manage a personal vehicle used by a TNC driver to provide prearranged rides.

The new Indiana law defines "TNC" to mean an entity that "(1) does business in Indiana; and (2) uses a digital network to connect TNC riders to TNC drivers to request prearranged rides." A "digital network" means "an online enabled application, software, web site, or system offered or used by a TNC to enable the prearrangement of rides with TNC drivers." Examples of TNCs likely could include Uber and Lyft.

H.B. 1278 does not expressly identify any specific purpose for which a driver's deemed independent-contractor status will apply.

Representative Matthew Lehman (R) introduced H.B. 1278 on January 22, 2015, and it was signed into law by Governor Mike Pence (R) on May 5, 2015.

C. Nevada

Nevada established a new statutory presumption that a worker is an independent contractor for purposes of the state's minimum-wage laws. The new presumption, contained in S.B. 224, became effective on June 2, 2015. The state otherwise uses the "economic realities" test to determine an individual's status for these purposes, which is the same test that courts use for purposes of the Fair Labor Standards Act.

S.B. 224 provides that an individual is "conclusively presumed" to be an independent contractor if:

> (a) Unless the person is a foreign national who is legally present in the United States, the person possesses or has applied for an employer identification number or social security number or has filed an income tax return for a business or earnings from self-employment with the Internal Revenue Service in the previous year;
>
> (b) The person is required by the contract with the principal to hold any necessary state or local business license and to maintain any necessary occupational license, insurance or bonding; and
>
> (c) The person satisfies three or more of the following criteria:

(1) Notwithstanding the exercise of any control necessary to comply with any statutory, regulatory or contractual obligations, the person has control and discretion over the means and manner of the performance of any work and the result of the work, rather than the means or manner by which the work is performed, is the primary element bargained for by the principal in the contract.

(2) Except for an agreement with the principal relating to the completion schedule, range of work hours or, if the work contracted for is entertainment, the time such entertainment is to be presented, the person has control over the time the work is performed.

(3) The person is not required to work exclusively for one principal unless:

(I) A law, regulation or ordinance prohibits the person from providing services to more than one principal; or

(II) The person has entered into a written contract to provide services to only one principal for a limited period.

(4) The person is free to hire employees to assist with the work.

(5) The person contributes a substantial investment of capital in the business of the person, including, without limitation, the:

(I) Purchase or lease of ordinary tools, material and equipment regardless of source;

(II) Obtaining of a license or other permission from the principal to access any work space of the principal to perform the work for which the person was engaged; and

(III) Lease of any work space from the principal required to perform the work for which the person was engaged.

S.B. 224 indicates that "the fact that a person is not conclusively presumed to be an independent contractor for failure to satisfy three or more of the criteria" set forth above, "does not automatically create a presumption that the person is an employee."

The Senate Committee on Commerce, Labor and Energy introduced S.B. 224 on March 6, 2015. On June 2, 2015, Governor Brian Sandoval (R) signed it into law.

D. South Dakota

South Dakota enacted a new law, H.B. 1105, that creates a rebuttable presumption that a person is not an employee for workers' compensation purposes. The new law amends the

Workers' Compensation law by adding a new section permitting "any independent contractor who is not an employer or a general contractor and is not covered under a workers' compensation insurance policy" to sign an affidavit of exempt status. The affidavit "creates a rebuttable presumption that the affiant is not an employee" for workers' compensation purposes. Generally, South Dakota follows a common law test to distinguish employees from independent contractors for these purposes.

According to H.B. 1105, a business that obtains an affidavit of exempt status from a worker is not required to make workers' compensation contributions on behalf of such worker. However, to deter any abuse of this provision, the new law provides "[a]ny person who solicits or provides false information on an affidavit of exempt status . . . with actual knowledge is guilty of a Class 2 misdemeanor."

Representative Spencer Hawley (D) and Senator Corey Brown (R) introduced H.B. 1105 on January 26, 2015, and on March 11, 2015, Governor Dennis Daugaard (R) signed it into law.

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If you have any questions or comments concerning the foregoing, please let us know.