

# Misclassification of Employees as Independent Contractors

Update to 2007 Evaluation Report

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## Problems Identified

- **Minnesota Employers Often Misclassify Employees as Independent Contractors.** An estimated 14 percent of Minnesota employers subject to unemployment insurance taxes, or 1 in 7, misclassified at least one worker in 2005.
- **Criteria for Determining a Worker's Classification Vary.** The departments of Employment and Economic Development (DEED), Revenue (DOR), and Labor and Industry (DLI) share state authority over classification of workers. State laws and rules, along with related judicial case law, establish somewhat different factors to be considered by each agency when determining a worker's status.
- **Weaknesses in Enforcement Activities by State Agencies.** DEED, DOR, and DLI's efforts to detect and deter misclassification ranged from very limited to modest, and they were not well coordinated.
- **Lack of Penalty for Repeated Misclassification.** Because of limits in state law, employers cannot be penalized specifically for misclassification of employees.

## Changes Implemented

- **Statutory Definition of Independent Contractor Clarified.** To improve consistency for worker classification in the construction industry, state unemployment statutes now refer to DLI's definition of independent contractor. DEED and DOR determined that the two agencies' definitions are sufficiently similar, requiring no changes.
- **Greater Information Sharing.** DEED and DOR have started routinely sharing audit information on worker classification determinations and conferring on audit strategies to avoid duplication. DLI is now using DEED employer payroll records to verify worker status in its investigations and plans to do more information sharing with DEED and DOR in the near future.
- **More Timely Access to Data on Payments to Independent Contractors.** DOR has joined a federal Internal Revenue Service program to gain more timely access to "Form 1099" data. Businesses use the form to report payments to independent contractors. This is expected to improve timely investigation of worker classification issues.

## Action Needed

- **Enact Provisions of HF885/SF681.** The Legislature should enact DOR's proposal to amend *Minnesota Statutes* 289A.60 (HF885/SF681), which would strengthen fiscal consequences for employers that misclassify workers and fail to withhold income tax as required. This includes contractors that are required to withhold income tax from payments to independent contractors.