



## Regulatory hammer strikes again

**By Gerald Faber**

Any business entity primarily engaged in the business of, or who enters into a contract for, “making improvements to real property” must have a clear understanding and follow the requirements of the Construction Industry Independent Contractor Act (CIICA). This legislation, one piece of a concerted effort to regulate the industry, seeks to end the practice of misclassifying employees as independent contractors, which deprives workers of legal benefits, the government of tax revenues and

competitors of an even-playing field.

The misclassified “contractor” is deprived of protections under wage and hour, unemployment, disability, workers compensation, whistleblower and anti-discrimination laws.

There can be severe consequences, including criminal convictions, for violations of CIICA, which is administered by the N.J. Department of Labor and Workforce Development. In addition, a violator may likely find itself in the midst of an enforcement storm by other agencies or individuals.

How do claims arise? The law provides for a private cause of action on behalf of an individual employed as a construction worker who has not been properly classified as an employee. The plaintiff may sue not only the contractor but any other employer in contract with the plaintiff for failing to properly classify the employee, if it had knowledge of the misclassification.

In addition, an individual representative, including a labor organization, may bring the action on behalf of the individual or as a class action. A successful plaintiff may be awarded attorney fees and other costs, in addition to individual or class damages.

A claim also may be triggered by a worker hurt on the job who is seeking workers compensation benefits, by a terminated worker applying for unemployment compensation or by an applicant for state disability benefits. A worker seeking health coverage also could trigger a claim. Investigation of wage and hour, whistleblower, discrimination or other employee protection claims may result in bringing actions under CIICA.

Tax agencies reclassify workers in order to increase revenue. For instance, Internal Revenue Service audits may be triggered by contractors who receive very few 1099-MISC Forms, by employers filing a large number of these forms compared to W-2 forms, issuing 1099-MISC Forms to the same person for

several years, or issuing 1099-MISC Forms to someone previously receiving W-2 forms. In addition, the construction industry as a whole has been targeted for tax audits. Moreover, federal and state taxing agencies have agreed to share employment tax examinations as part of an overall attempt to centralize data for use by state and federal taxing authorities.

The Department of Labor and Workforce Development also has increased its oversight and has an information-sharing agreement with the state Division of Taxation. Complaints by business competitors also may spark investigation and enforcement by the Labor Department.

Who is covered by the law? The term “employer” is defined as a business entity who is “primarily engaged in the business of, or enters into a contract for, making improvements to real property.” Proposed regulations under the law will clarify that individuals also are covered. While the term “making improvements” is not further defined, it should encompass all the activities within the definition of “home improvement” captured in the Contractors Registration Act, N.J.S.A. 56: 8-136. That law covers residential structural repairs, remodeling and cosmetic improvements, as well as work on the grounds and fixtures.

### Broader coverage

This law’s coverage is broader as it does not specifically exclude “commercial”

real property. In addition, new-home builders should be covered as the term “employers in the construction industry” is not further refined.

The law deems the status of an individual who performs services for pay in the making of improvements to real property as “employment” unless and until it is shown to the satisfaction of the Labor Department that the individual

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meets the tests to be deemed an independent contractor, with respect to enforcement of the following laws:

- The New Jersey Prevailing Wage Act, P.L.1963, c. 150 (C.34:11-56-25.)
- The Unemployment Compensation Law, R.S.43:21-1
- The Temporary Disability Benefits Law, P.L.1948, c. 110 (C.43:21-25.)
- The New Jersey Gross Income Tax Act, N.J.S. 54A:1-1
- Other applicable state tax laws, P.L.1965, c. 173 (C.34:11-4.1.)
- The New Jersey State Wage and Hour Law, P.L.1966, c. 113 (34:11-56a.)
- N.J.S.A. 34:20-4

The presumption of employment can only be overcome by passing the “ABC test”:

A. The individual has been and will continue to be free from control or direction over

the performance of that service, both under his contract of service and in fact; and

B. The service is either outside the usual course of business for which the service is performed, or the service is performed outside all the places of business of the employer for which the service is performed; and

C. The individual is customarily engaged in an independently established trade, occupation profession or business.

It is important to underscore the fact that under the ABC test, each prong must be met to establish an independent contractor relationship.

The control test contained in the “A” prong is derived from common law. Traditionally, an employment relationship will exist if the employer exercises “control” or has the “right of control” over the methods and quality of a worker’s performance. The greater the exercise of control, the greater the chance the worker will be deemed an employee.

The Restatement, Agency 2d (1958) sets forth the essential elements of the common law “right of control” test:

(a) The extent of control which, by the agreement, the master may exercise over the details of the work;

(b) Whether the one employee is engaged in a distinct occupation or business;

(c) The kind of occupation, with reference to whether, in the locality, the work is done under the direction of the employer or by a specialist without supervision;

(d) The skill required in the particular occupation;

(e) Whether the employer or workman supplies the instrumentalities, tools and place of work for the person doing the work;

(f) The length of time for which the person is employed;

(g) The method of payment, whether by the time or by the job;

(h) Whether the work is part of the regular business of the employer;

(i) Whether the parties believe they are creating the relationship of master and servant; and

(j) Whether the principal is or is not a business.

With respect to the “B” prong, a contractor might argue this prong is met because contracting jobs are performed outside the employer’s place of business. In the 1942 case *Superior Life, Health and Accident Ins., Co. v. Bd. of Review of the Unemployment Compensation Commission*, 127 NJL 537, the New Jersey Supreme Court found the place of business of an insurance company was any place within the area where policyholders were located and where new business was to be solicited. As such, this argument would likely fail.

## Independence

Independence is the hallmark of the “C” prong. This concept is thoroughly explored in cases interpreting New Jersey’s Unemployment Compensation Act, which applies the same test to determine employment. Factors include duration and strength of the business, number of employees, organization of the business, separate clients, use of own stationery and contact information, use of assets, advertising, and amounts of time devoted to company work.

Clearly, the law requires an in-depth analysis of the relationship. Agreements that merely parrot the test factors will be rejected if the true situation does not withstand scrutiny. The law specifically prohibits an employer from making an agreement that results in the misclassification of a worker.

Penalties for violation of the law vary based on a contractor’s level of culpability and size of contract. An employer

or responsible agent of the employer who fails to properly classify an individual as an employee and who fails to pay wages, benefits, taxes or other contributions as required by the relevant laws are subject to the following criminal liability:

1. Irrespective of intent, a disorderly persons offense, subject to a fine of not less than \$100 and no more than \$1,000, or imprisonment for not less than 10 nor more than 90 days, or both. Each week, in any day of which an employee is misclassified and each employee so classified, shall constitute a separate offense.

2. If the failure is done knowingly, a second-degree crime, if the contract amount is for \$75,000 or above; a third degree crime if the contract amount exceeds \$2,500 but is less than \$7,500; and a fourth-degree crime if the contract amount is \$2,500 or less. If convicted, the violator shall be deemed to have caused loss to the employees in any amount by which the employees were unpaid in connection with the misclassification. Further, the convicted shall be subject to the provisions of N.J.S.A. 2C:43-3 (fines and restitutions to victims) and other Title 2C provisions, including N.J.S.A. 2C:43-4 (penalties and forfeitures against corporations), 2C:43-6 (terms of imprisonment) and 2C:44-1 (criteria for sentencing).

In addition, administrative penalties up to a maximum \$2,500 for a first violation and a maximum \$5,000 for each subsequent violation may be levied. Factors in determining the amount of the penalty include history of previous violations, seriousness of the violation, good faith of the employer and size of the employer’s business. Of course, the employer is afforded due process with respect to the penalties.

## Prohibition

Those who knowingly fail to properly classify an individual and pay required contributions or who are convicted of second, third- or fourth-degree crimes pursuant to the law shall be debarred from public contracting for three years. This prohibition also is subject to due process accorded the employer.

The law confers the additional power to immediately suspend the contractor's registration, issued pursuant to N.J.S.A. 34:11-56.54 (public works contracts), even if the violation was not knowingly committed. This action must be based on a determination that ordering an immediate suspension is in the public interest and is subject to the contractor's due process rights.

For a second violation, the commissioner shall issue a stop-work order requiring cessation of all business operations at every site at which the violation occurred within 72 hours of the determination. Proposed regulations clarify that the sanction applies to the business operations "of the violator." The stop-work order will not be released until the employer has properly classified the individual and paid any penalty assessed under the section. The employer also may be placed on a probationary period for no more than two years, requiring it to file periodic reports demonstrating its continued compliance with the law.

For third or subsequent violations, the stop-work order shall be issued for all the violator's business operations within 72 hours of the

determination. The order may be released in the same fashion as with second violations.

A civil penalty of \$5,000 per day may be issued against an employer for each day it conducts business operations in violation of a stop-work order as to each individual the employer fails to properly classify.

CIICA also contains a provision making it unlawful to retaliate for the exercise of rights under the law or for assisting a claimant. Any adverse action within 90 days of the exercise of rights raises a rebuttable presumption of retaliation.

It must be emphasized that any business is exposed to separate liability for misclassification of workers under myriad other laws, many of which apply different tests or variations of the ABC test. Examples include Internal Revenue Service and other tax laws, Conscientious Employee Protection Act, New Jersey Law Against Discrimination, Fair Labor Standards Act, Americans with Disabilities Act, Title VII of the Civil Rights Act of 1964, Age Discrimination in Employment Act, National Labor Relations Act, Immigration and Control Act, and Employee Retirement Income Security Act.

## Steps to take

The following steps are recommended to avoid misclassifying independent contractors as employees:

1. Review and follow the factors in the ABC test and interpretive cases.
2. Do not utilize independent contractors to do the work the business performs,

in the absence of special circumstances.

3. Procure confirmation from independent contractors as to their independent status, such as:

- A. Proof the concern is an incorporated business;
- B. Proof of workers compensation, general liability and other insurance coverage; and
- C. Copies of advertising brochures, cards and other promotional materials.

4. Obtain various bids on projects and have the chosen independent contractor submit a proposal on a form, which is fully compliant with the New Jersey Contractor's Registration Act.

5. Do not give company materials to an independent contractor to distribute or allow contractor to represent himself as an agent or company employee.

6. Do not give contractor company property for business use, including tools, electronic technology or credit cards.

7. Keep contractor's compensation separate from employees. Do not allow contractor to be eligible for any company benefits or events.

Finally, a business should have written agreements with contractors that memorialize essential terms of the contract, including events of termination. Acknowledge the fact the company is under no obligation to treat the contractor as an employee. A contractor should acknowledge that it employs its own workers and is responsible for all attendant obligations. The contractor should acknowledge and submit proof of its own pertinent insurance coverage and licenses. ©



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