



Robert W. Wood

THE TAX LAWYER

TAXES 10/20/2017

When 'Independent Contractors' Get Unemployment Benefits, What It Means For Employers

With Uber, Lyft, and many other companies that provide many different services and products, the norm these days seems to be independent contractors. The companies avoid the huge taxes, expenses, and liabilities of having employees. The workers get the freedom to work on their own, managing their own schedules. One of the great unanswered questions, of course, is how much control is too much for independent contractors, without making them employees. Many

lawsuits brought by workers and by third parties are about this very question.



With true independent contractors, of course, there is no employment relationship, no employment taxes, no workers' compensation coverage, and no unemployment insurance. Let's just take that last item.

Unemployment benefits are only for people who are (or were) employed as employees. Yet you might be surprised that unemployment benefits sometimes go to workers who were actually independent contractors and not employees, at least by name. How can this happen?

A terminated independent contractor applies for unemployment benefits. The company that previously paid the independent contractor may not contest the claim. Even if the company contests the claim, the unemployment authority in question may rule in the worker's favor awarding the benefits. After all, the lines can blur between independent contractors and employees. Assume that the employer has a written agreement agreeing to independent contractor status. Even so, the agency can rule for the worker. The reclassification to employer-employee might be effective only for unemployment purposes. But that's all it takes for the worker to get unemployment benefits.

Some employers flatly abuse the "independent contractor" label. Recharacterizing the worker is plainly appropriate in some cases. But some unemployment benefits are paid to people who truly were independent contractors and who probably should not be recharacterized in this way. How do you tell if someone is an employee regardless of what they may be called? It's not easy. The IRS factors are widely used and based on common law determinations of control. Most unemployment tests are much more weighted in favor of finding employee status. In fact, there are many different tests in play, and that can be confusing.

The risk to companies from these characterization questions can be significant. In some cases, there can even be criminal liability. For employers who have other workers in the same "independent contractor" category as the worker claiming benefits, even a simple unemployment claim can be the first domino to fall that may trigger others. Agencies exchange information, and one dispute often leads to others.

A very small dollar amount of unemployment benefits can end up leading to massive other liabilities. The status of a worker as an independent contractor or an employee is important for federal income and employment taxes (think IRS and Social Security Administration). It also affects state income and employment taxes. Then there's the U.S. Department of Labor and the state counterpart agencies. Many states have Departments of Industrial Relations, OSHA agencies, and more.

Then, there are also pension and fringe benefit issues, involving both governmental agencies (many are jointly administered by the IRS and the Department of Labor), private parties and insurance companies. Another big category is workers' compensation benefits. Despite the generic "worker" name, workers' compensation benefits almost invariably are only for employees, not for independent contractors. Characterization questions—*is this injured worker really an independent contractor or an employee*—occur all the time.

Civil liability (for accidents or injuries the worker might cause) can also be dramatically different. You generally are not liable for injuries your independent contractor causes while working for you. In contrast, for acts of your employees, you have full liability. The bottom line? If you're an employer and have

independent contractors, you should consider how strong your written agreement is with your contractors, and how closely you follow it. When deciding whether to contest claims, consider the potential domino effect in the future.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.