



Employee misclassification

Employee vs. independent contractor under 181.722 – general misclassification

- Determined using existing workers' compensation and unemployment tests.
- Outside of construction, tests have not been changed and primarily rely on balancing identified factors.
- Applies to workers outside the construction industry.
- Independent contractor tests contained in Minnesota Rules 5224 and 3315.0555.
- General workers' compensation test in Minnesota Rules 5224.0320 to 5224.0340.
- Certain occupations have their own workers' compensation criteria established in 5224.



Workers' compensation test: The control factor – 5224.0330



Control over assistants;



Compliance with instructions;



Oral or written reports;



Place of work;



Personal performance;



Existence of continuing relationship;



Set hours of work;



Training;



Amount of time;



Simultaneous contracts;



Tools and materials;



Expense reimbursement; and



Satisfying requirements of regulatory and licensing agencies.

Workers' compensation test: Other factors – 5224.0340

 Right to discharge;

 Availability to the public;

 Compensation on a job basis;

 Realization of profit or loss;

 Right to terminate;

 Substantial investment;

 Responsibility; and

 Services fundamental to the business.

Unemployment test – 3315.0555

- The right or lack of the right to control the means and manner of performance;
- Right to discharge the worker without liability for damages;
- Mode of payment;
- Furnishing of materials and tools;
- Control over the premises where services are performed; and
- Other factors if necessary.

Prohibited activities

1. Failing to classify, represent, or treat an employee as an employee in accordance with the requirements of any law;
2. Failing to report or disclose an employee to any government agency when required to do so under the applicable law; and
3. Requiring or requesting an employee to enter into any agreement or complete any document that misclassifies, misrepresents, or treats the individual as an independent contractor, or otherwise does not reflect the individual is an employee.

Best practices

- Review Minnesota Rules 3315.0555 and 5224.0320 to 5224.0340 for more detailed explanation of factors.
- Review Minnesota Rules 5224.0020 to 5224.0312 for criteria for specific occupations subject to their own test.
- Use written contracts with independent contractors.
- Do not control, in contract or in fact, the details of an independent contractor's work, keep the focus on the end result.
- Clearly define the scope of services and the payment.
- Avoid classifying workers as independent contractors if they perform the same work as employees or work integral to your business.
- Ensure compliance with tax laws.



Misclassification in construction industry

Scope

- Applies to residential and commercial building construction and improvement services only.
- Does not apply to highway/heavy construction or most landscaping work.
- Applies to individuals performing or providing services for a person that are “in the course of the person’s trade, business, profession, or occupation ...”



Independent contractor test

- Minnesota Statutes section 181.723, subdivision 4.
- Effective for services provided or performed on or after March 1, 2025.
- Many elements are the same as or similar to previous elements.
- Like the previous test, there is a presumption of employment. All elements must be met to establish independent contractor status. Not a balancing test.
- Focuses on two primary inquiries: (1) is the engaged person operating a legitimate and separate business, and (2) does a legitimate contract exist?

Legitimate and separate business (1-3)

1. Established and maintained separately and independently from the person for whom the services are provided or performed;
2. Owns, rents, or leases, equipment, tools, materials, supplies, office space, or other facilities that are used to provide or perform the services;
3. Provides, performs, or offers the same or similar services for multiple persons or to the general public;

Legitimate and separate business (4)

4. Is in compliance with the following:
 - i. holds a federal employer identification number if required;
 - ii. holds a Minnesota tax identification if required;
 - iii. has received and retained 1099s for income received for construction services if required;
 - iv. has filed business or self-employment taxes for construction services, if any, in the previous 12 months; and
 - v. has completed a W-9 to the person for whom the services were performed.

Legitimate and separate business (5-8)

5. Is in good standing with the Minnesota Secretary of State, if applicable;
6. Has a Minnesota Unemployment Insurance account, if required;
7. Has obtained workers' compensation coverage, if required;
8. Hold current business licenses, registrations, and certifications, if required by chapter 326B or sections 327.31 to 327.36;

Legitimate contract (9)

9. Operating under a written contract to perform specific services that:
 - i. is signed and dated by an authorized representative of both business entities;
 - ii. is fully executed no more than 30 days after the work commences (not required for change orders);
 - iii. identifies the specific services to be performed; and
 - iv. provides for compensation on a commission, per-job, or competitive bid basis and not on any other basis.

Legitimate contract (10-11)

10. Submits invoices and receives payments in the name of the business entity.
Cash payments do not meet this requirement;
11. Terms of the contract provide the engaged entity with control over the means of providing the services and the engaged entity exercises control in fact;

Legitimate contract (12-14)

12. Incurs the main expenses and costs related to performing the services under the contract;
13. Is responsible for the completion or failure to complete the services under the contract; and
14. May realize additional profit or suffer a loss under the contract if costs and expenses are greater or less than the contract price.

Upper-tier employee-employer relationship

- An upper-tier contractor will be the employer of any worker performing or providing services in the contracting chain below unless an intervening business entity and contract meet the test; and
- An employment relationship will not be created between an upper-tier contractor and worker performing services at a lower tier if an intervening business entity properly treats and classifies the individual as an employee in accordance and in compliance with applicable laws.



Prohibited activities, continued

- Requiring an employee to register as a contractor, agree to be treated as an independent contractor, or form a business entity as a condition of payment.
- Failing to classify, represent, or treat an employee as an employee in accordance with the requirements of chapters 176, 177, 181, 181A, 182, 268, and 326B.
- Failing to report or disclose an employee when required to do so under law.
- Requiring or requesting that an employee enter into an agreement or complete a document that misclassifies, misrepresents, or treats the individual as an independent contractor or otherwise does not reflect that the individual is an employee.
- Requiring an employee to register under section 326B.701.

Individual liability

The following may be held individually liable for knowingly or repeatedly engaging in prohibited activities on behalf of the employer:

1. owners;
2. partners;
3. principals;
4. members;
5. officers; and
6. agents.



Successor liability

- Orders for engaging in prohibited activities are effective against a successor business;
- A successor business is anyone meeting three or more of the following criteria:
 1. Has one or more same owner; member, principal, officer, or manager;
 2. Performs similar work within Minnesota;
 3. Has one or more of the same telephone or fax number;
 4. Has one or more the same email addresses or websites;
 5. Employs or engages substantially the same individuals to provide or perform services;
 6. Utilizes substantially the same vehicles, facilities, or equipment;
 7. Lists or advertises substantially the same project experience or portfolio of work.

Damages and penalties (1)

1. Compensatory damages to the misclassified worker resulting from the failure to classify, represent, or treat the individual as an employee; including, but not limited to:
 - Supplemental pay including minimum wage, overtime, shift differentials, vacation pay, sick pay, and other paid time off;
 - Health insurance, life and disability insurance;
 - Retirement plans, savings plans and any other form of benefit;
 - Employer contributions to unemployment insurance; Social Security and Medicare, and any costs and expenses incurred by the individual resulting from the failure to classify, represent, or treat the individual as an employee.

Damages and penalties (2-4)

2. Up to \$10,000 penalty for each worker the person failed to properly classify, represent, or treat as an employee;
3. Up to \$10,000 penalty for each violation of section 181.722, subdivision 1 or section 181.723, subdivision 7;
4. Up to \$1,000 penalty for any person who delays, obstructs, or otherwise fails to cooperate with the investigation. Each day of delay, obstruction, or failure to cooperate is a separate violation.

Factors DLI must consider in determining penalty amounts – section 14.045, subd. 3.

- Willfulness of the violation;
- Gravity of the violation, including damage to humans, animals, and the natural resources of the state;
- History of past violations;
- Number of violations;
- Economic benefit gained by the person by allowing or committing the violation;
- Other factors that justice may require; and
- For a violation other than an initial violation: similarity or previous violations, time elapsed since last violation, number of previous violations, response of the person to the most recent previous violation identified.

Additional best practices

- Be mindful of record-keeping requirements – must keep documents and information independent contractor determination was based on for at least three years;
- Consider whether your subcontractor will provide documents and respond to the department in the event of an investigation;
- Remember the test applies to change orders as well; change orders cannot be used to disguise that the test is not met – reasons for legitimate change orders should be identifiable;

Additional best practices, continued

- Ensure subcontractors have responsible forepersons or supervisors who direct details of their work;
- Ensure written contracts accurately reflect the nature of the relationship and obligations of the parties; and
- Document contract negotiations.

Enforcement example: Merit Drywall (allegations from criminal complaint)

- Paying individuals entirely on piece rate or hourly basis.
- Individuals wore uniforms of hiring contractor.
- Individuals were subject to extensive supervision and direction by hiring contractor.
- Individuals were paid in cash under the table.
- Hiring contractor established companies and arranged minimal insurance for individuals.
- Hiring contractor supplied overwhelming majority of materials.
- Through misclassification hiring contractor evaded hundreds of thousands of dollars in workers' compensation premiums.

Stop-work orders – Generally

- Change effective March 1, 2025.
- Similar to stop order authority of department under existing law.
- May be issued to a person who has engaged in specific conduct based on inspection or investigation.
- Provides for expedited appeal.
- Affected employees entitled to up 10 days of backpay for missed work.
- Penalties for violation of stop-work order.
- 14.045 factors must be considered when determining whether stop-work should be issued and scope of order.
- Grounds for stop-work orders include violations of applicable laws.



Thank you