NELSON HARDIMAN
HEALTHCARE LAWYERS

New California Law Targets Employers Who Misclassify Employees As Independent Contractors

On October 9, 2011, Governor Jerry Brown signed SB 459 — a new law which imposes stiff penalties on employers who willfully misclassify employees as independent contractors. SB 459 exposes employers to civil damages, liquidated damages, and civil penalties between $5,000 and $25,000 per violation. SB 459 also provides violators with a Scarlet Letter (notice to the public), which must remain posted on the employer's website for one year.[1]

All employers should be concerned about their exposure under this new law. Innocent or mistaken misclassifications might be deemed unlawful. SB 459 uses a broad "willful misclassification" standard to determine whether a misclassification is unlawful. This means that, to violate the law, the misclassification must have been done "voluntarily and knowingly." While this standard certainly encompasses intentional misclassifications by employers with actual knowledge, it also includes misclassifications by employers with constructive knowledge, meaning employers who should have known that the misclassification was unlawful. With such broad potential for exposure, employers must make sure that their classifications are correct.

In recent years, we have seen more employment disputes where former independent contractors claim they were misclassified. Independent contractors who are suddenly terminated or who feel they were underpaid for their services are usually the culprits behind a claim for misclassification. Obviously, employers who contract with a large number of independent contractors have a greater potential for exposure. However, SB 459 presents an opportunity for all employers to review whether they are classifying their workers properly.

In order to avoid an adverse determination, employers should perform a self audit of their current worker classifications. Preferably, employers should do this with the assistance of counsel. However, since retaining counsel might not be possible, employers should become familiar with how to properly classify a worker's status.

The IRS has published the common law balancing test to help employers determine worker status. This test examines the following three aspects of the work-relationship: behavior control, financial control, and type of relationship. The most important question underlying this analysis is how much control does the employer retain over the worker. If the employer retains a great degree of control, then the worker might be an employee. However, it should be noted that no one factor in the common law test is determinative. Employers should keep in mind that a worker's classification is based on a totality of the circumstances.

While SB 459 is victory for independent contractors seeking to enforce their rights, SB 459 may catch many California employers off guard. Nelson Hardiman routinely counsels health care providers on employment issues, including drafting employment agreements, drafting independent contractor agreements, and structuring worker relationships to comply with state and federal law. Please contact Nelson Hardiman if you would like to schedule a consultation to discuss your employment issue.

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[1]Upon receiving an adverse determination, the employer must prominently display, on its website or an area accessible to the general public, a notice that sets forth the following: (1) the employer has committed a serious violation of the law by engaging in the willful misclassification of employees; (2) the employer has changed its business practices to avoid further violations; (3) any employee who believes that he or she is being misclassified as an independent contractor may contact the Labor and Workforce Development Agency; and (4) the notice is being posted pursuant to a state order. Employers who are convicted of a violation must post this notice for one year.