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## Pennsylvania Passes Construction Worker Misclassification Act with Broad Scope, Criminal Penalties and Strong Whistleblower Protection

Pennsylvania recently joined a growing number of other states that have enacted laws establishing explicit criteria – and penalties – governing the classification of workers as independent contractors. Pennsylvania’s Construction Workplace Misclassification Act, effective in February 2011, sets forth criteria for determining whether workers in the construction industry are independent contractors or employees for purposes of workers’ compensation and unemployment compensation laws. It imposes civil and criminal penalties for the misclassification of construction workers as independent contractors when they should be considered employees, as well as penalties for retaliation against someone who reports a misclassification. Those who face penalties include not only employers, but also their officers and agents and those who knowingly contract with another employer violating this law. This sweeping legislation will have broad impact on employers involved in a widely construed interpretation of the construction industry, whether or not engaged in public works.

### Independent Contractor Criteria

As described below, the law narrowly defines an independent contractor for purposes of workers’ compensation and unemployment compensation laws.

An individual who performs services for remuneration in the construction industry can be considered an independent contractor only if he or she (1) has a written contract to perform the services, (2) is free from control or direction over performance of the services, both under the contract and in fact, and (3) is customarily engaged in an independently established trade, occupation, profession or business with respect to the services performed.

To be “customarily engaged in an independently established trade, occupation, profession or business,” the individual must:

1. possess the essential tools, equipment and other assets necessary to perform the services independent of the person for whom the services are performed;
2. have an arrangement in which he or she realizes a profit or suffers a loss as a result of performing the services;
3. perform services through a business in which he or she has a proprietary interest;
4. maintain a business location that is separate from the location of the person for whom services are performed;

5. have previously performed the same or similar services for another person, in accordance with (1) through (4) above, while free from direction or control over performance of the services OR must hold himself or herself out to other persons as available and able – and must be available and able – to perform the same or similar services in accordance with (1) through (4) above, while free from direction or control over performance of the services; and
6. maintain at least \$50,000 in liability insurance during the term of the contract.

The law makes clear that failure to withhold income taxes, to contribute to unemployment compensation, or to pay workers' compensation premiums for someone should not be considered when determining whether that person is an employee or an independent contractor in the construction industry.

It is also worth noting that the law broadly defines "construction" to include erection, reconstruction, demolition, alteration, modification, custom fabrication, building, assembling, site preparation and repair work done on any real property or premises under contract, irrespective of whether the work is done for a public body and paid for from public funds.

### Whistleblower Protection

The new law prohibits retaliation against an individual who exercises any rights under the law, including filing a complaint or informing any person about an employer's noncompliance with the law. Even someone who files a complaint and does not prevail is protected from retaliation so long as the allegations were made in good faith. If any adverse action is taken against someone within 90 days after the individual alleged a violation of the law, there is a presumption that the action was retaliatory. While that presumption can be rebutted, it places a burden on the employer to show that the action was based on a legitimate, non-retaliatory reason. A violation of this whistleblower provision is considered a separate violation, subject to the same penalties as a misclassification, which are described below.

### Penalties

An employer, or an officer or agent of an employer, is subject to penalties if it misclassifies an employee as an independent contractor for purposes of workers' compensation or unemployment compensation, and can be charged with a separate violation for each employee misclassified. However, there is a good faith defense available if the person for whom the services are performed believed, in good faith, that the employee qualified as an independent contractor at the time he or she performed the services.

An intentional misclassification is a misdemeanor of the third degree (carrying a penalty of up to 12 months imprisonment and fines of up to \$2,500). It could also lead to a court order requiring any misclassified employee to cease work within 24 hours and, if the majority of workers at the site are misclassified, could shut down that employer's operations at the site. A negligent misclassification is a summary offense subject to a fine of not more than \$1,000. The Department of Labor & Industry can also assess civil penalties of up to \$1,000 for the first violation and up to \$2,500 for later violations. The following factors are considered in determining the amount of the civil penalty: the history of previous violations by the employer, the seriousness of the violation, the good faith of the employer, and the size of the employer's business.

In addition, the law extends its penalties to parties that are not employers, or officers or agents of an employer. A party that intentionally contracts with an employer knowing the employer intends to misclassify employees in violation of the law is subject to the same penalties as the employer.

### Conclusion

This law, which will take effect in February 2011, makes it imperative that employers in Pennsylvania's construction industry closely examine their contracts and relationships with all purported independent contractors. The construction industry is one that has wrestled with issues involving classification of independent contractors for many years. Recently, however, the issue whether individuals are independent contractors or employees has received significant

attention across the board, as seen with proposed state and federal legislation, agency enforcement efforts, and litigation activity. For example, New York, which just this fall enacted “The New York State Construction Industry Fair Play Act,” created a multi-agency task force on employee misclassification that found \$607 million in alleged unreported wages and 44,000 purportedly misclassified employees in various industries over the past three years. The U.S. Department of Labor’s Wage and Hour Division collected \$2.6 million for misclassified employees last year and is

seeking \$25 million in its 2011 budget to target misclassification.

Employers in construction and other industries need to be mindful when deciding to engage workers as independent contractors, and make certain that their decisions comply with all applicable laws, including state and federal tax laws, wage and hour laws, and laws imposing requirements with respect to employees. In Pennsylvania, employers in the construction industry now have one more important reason to proceed with caution in this area.

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