



Employment Case Studies:

Misclassification of Employees as Independent Contractors

Provided by **Tim Keogh/ACNB Insurance Services**





Introduction

When a worker is classified as an employee rather than an independent contractor, they are entitled to minimum wage and overtime pay protections under the Fair Labor Standards Act (FLSA). Enforced by the U.S. Department of Labor (DOL) Wage and Hour Division, the FLSA establishes minimum wage, overtime pay, recordkeeping, and youth employment standards affecting employees in the private sector and in federal, state and local governments.

This article provides a general overview of the difference between employees and independent contractors. It also contains case studies that provide real-world examples of employers found to be in violation of FLSA regulations due to independent contractor misclassifications and offers guidance for how those employers could have prevented these infractions. By examining these case studies, employers can learn from the mistakes of others in similar industries and avoid FLSA violations related to the misclassification of independent contractors.

Key Differences Between Employees and Independent Contractors

In practice, it is critical for employers to understand the difference between independent contractors and employees under the FLSA. Generally, a worker is an employee when the employer exercises greater control over how the work is completed; conversely, an independent contractor chooses how to complete the job at their own discretion. The Wage and Hour Division’s role is to determine whether an employee is misclassified as an independent contractor and, thus, has been denied the wage, benefits and labor standards protections they are entitled to under the FLSA.

The following is [guidance from the DOL](#) that clarifies the difference between employees and independent contractors:

Employee	Independent Contractor
Works for someone else’s business	Runs their own business
Receives hourly, salary or piece rate pay	Receives pay upon completion of the project
Uses employer’s materials, tools and equipment	Provides own materials, tools and equipment
Typically works for one employer	Works with multiple clients
Continues relationship with the employer	Maintains temporary relationship with employer until project is completed
Is instructed by the employer on when and how the work will be performed	Decides when and how they will perform the work
Is assigned work to be performed by the employer	Decides what work they will do

Additionally, the Internal Revenue Service (IRS) also provides guidance on the distinction between employees and independent contractors because that determination has an effect on taxes. For employees, employers generally need to withhold some pay for taxes, whereas with independent contractors, that is often not the case. According to the agency, firms and workers can file [Form SS-8](#) to request a determination of the status of a worker for purposes of federal employment taxes and income tax withholding. The IRS will review the facts and circumstances and officially determine the worker’s status.

For more information on this topic, visit the IRS resource [“Independent Contractor \(Self-Employed\) of Employee?”](#)

Real-world Case Studies



HOUSTON—An auto services company paid \$166,435 in back wages for 106 workers who were misclassified as independent contractors and therefore deprived of full benefits, wages and overtime pay.

What went wrong:

- The employer paid the affected workers straight time for all hours worked, but they worked more than 40 hours per week, which meant they did not receive the overtime pay to which they were entitled.
 - The employer did not maintain accurate records as required by the FLSA.
-



HOUSTON—A welding and fabrication company paid \$178,359 in back wages for 27 employees because they misclassified the workers as independent contractors and denied them their full wages and benefits.

What went wrong:

- The employer paid workers straight time when they worked well over 40 hours per week, which warrants overtime pay.
 - The employer failed to provide the required benefits to which full-time workers are entitled.
-



PLEASANT GROVE, UTAH—An auto body shop wrongly classified 13 workers as independent contractors and will pay \$47,175 in back wages.

What went wrong:

- The employer failed to pay workers overtime pay as is required for employees under the FLSA.
- The employer did not keep accurate employee pay and times records.

Correcting the Problems



Identify the Type of Worker

The reoccurring issue seen across all of these case studies was the failure to properly identify a worker as an employee. Even in the situation where relatively few workers were misclassified as independent contractors, the fines associated were still hefty. Employers should be cognizant of the types of workers they employ and classify them correctly so they can ensure they are properly handling matters with respect to each worker.



Pay Overtime

Another common issue in these case studies was the failure to provide overtime pay to workers. Employees covered by the FLSA must receive overtime pay for hours worked in excess of 40 in a workweek of at least 1.5 times their regular rates of pay.



Record Hours Diligently

According to the DOL, records must include accurate information about the employee and data about the hours worked and the wages earned. Real-world examples from the DOL highlight that when employers have wrongfully recorded hours, they are at risk of violations. This then leaves them subject to pay the unpaid wages and likely other larger fines. Employers should also be sure to follow all other applicable rules, laws and regulations on pay cycles, such as those concerning biweekly versus weekly pay.

Conclusion

These case studies demonstrate the significant financial consequences that result from misclassifying workers. However, these cases should not be viewed as dispositive when determining if an organization is in compliance with the FLSA. If employers are concerned their organization is not in compliance with the FLSA, they should seek legal advice.

While distinguishing between an employee and an independent contractor can be nuanced, the consequences of failing to do so can be costly. As the case studies show, most mistakes stem from the failure to follow the requirements laid out by the FLSA, and employers can learn from other organizations' failure to adhere to the rules. Further, federal resources can help employers understand the defining differences.

Employers should continue to monitor the FLSA and related changes that may occur. For additional guidance, explore the [DOL website](#), and contact us for more information regarding the FLSA.

*The information in this article is not intended to be construed as legal or professional advice. Employers seeking legal advice should speak with legal counsel.
© 2022 Zywave, Inc. All rights reserved.*

