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New York State Takes Aim at Independent Contractors in the Construction Industry

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On June 28, 2010, the New York State Legislature passed the New York State Construction Industry Fair Play Act (the "Act") aimed at correcting the misclassification of employees in the construction industry. The Act amends the New York Labor Law by adding a new article 25-A which creates a rebuttable presumption that all construction workers are employees. In addition, the Act amends New York's Unemployment Insurance Law and the Workers' Compensation Law incorporating, respectively, the presumption of employee status concerning construction workers under each of those laws. The act awaits Governor Patterson's signature and will become effective within sixty (60) days after its enactment.

The Act follows on the heels of numerous reports of widespread worker misclassification throughout the United States economy. Most recently, studies of New York City's construction industry alone suggest that nearly one in four workers – upwards of fifty thousand construction workers – are either misclassified as independent contractors or are paid completely "off the books," resulting in reductions in tax revenues. Such unlawful behavior also shifts the burden of taxes, unemployment insurance, and workers' compensation costs to law-abiding employers and workers, and lowers working conditions by excluding such workers from protective labor legislation.

In addition to creating a presumption of employment status, the Act requires a detailed notice posting (verbiage to be determined by the Commissioner of Labor), subjects contractors to civil penalties for violating the Act, provides for coordination by the Commissioner of Labor, Chair of the Workers' Compensation Board, and the Commissioner of Taxation and Finance with respect to violators, and subjects any contractor who "willfully fails to properly classify an individual as an employee" to both criminal and civil sanctions under the Act, as well as to penalties currently existing under New York's Unemployment Insurance, Workers' Compensation, and tax laws.

Summary of Specific Provisions

The Act defines construction as "constructing, reconstructing, altering, maintaining, moving, rehabilitating, repairing, renovating or demolition of any building, structure, or improvement, or relating to the excavation of or other development or improvement to land." In addition, a contractor is intended to include "any sole proprietor, partnership, firm, corporation, limited liability company, association or other legal entity. . .". A "contractor" includes a general contractor and/or subcontractor.

Presumption of Employment in the Construction Industry

Under new Article 25-A, construction workers performing work for a contractor will be classified as employees *unless* the person is a "separate business entity under subdivision two," or all of the following criteria are met: (a) the individual must be "free from control and direction in performing the job, both under his or her contract and in fact;" (b) the service provided "must be performed outside the usual course of business for which the service is performed;" and (c) the individual must be "customarily engaged in an independently established trade, occupation, profession, or business that is similar to the service at issue." If all these requirements are met the construction worker will be classified as an independent contractor.

The Act also provides for a "business entity" exception thereby allowing a sole proprietor, partnership, corporation, or person to be classified as an independent contractor provided the entity satisfies the Act's elaborate twelve-part test for a separate business entity. Thus, for a business entity to be considered an independent contractor, it must:

1. perform the service free from the direction or control over the means and manner of providing the service, subject only to the right of the contractor for whom the service is provided to specify the desired result;
2. not be subject to cancellation or destruction upon severance of the relationship with the contractor;
3. have a substantial investment of capital in the business entity beyond ordinary tools and equipment and a personal vehicle;
4. own the capital goods and gain the benefits and bear the losses of the business venture;
5. make its services available to the general public or the business community on a continuing basis;
6. include services rendered on a Federal Income Tax Schedule as an independent business or profession;
7. perform services for the contractor under the business entity's name;
8. obtain and pay for a license or permit in the business entity's name when such are required;
9. furnish the tools and equipment necessary to provide the service;
10. hire its own employees without contractor approval, pay the employees without reimbursement from the contractor, and report the employees' income to the Internal Revenue Service;
11. not represent the business entity as an employee of the contractor to the contractor's customers; and
12. have the right to perform similar services for others on whatever basis and whenever it chooses.

Notice and Posting Requirements

Contractors are now required to post a statement from the Commissioner of Labor in a conspicuous place on the work site, which details protections against retaliation, the penalties proscribed for improper classification of workers, the responsibilities of independent contractors, the rights of employees to unemployment insurance benefits, workers' compensation, minimum wage, and other federal and state workplace protections. The notice must also contain contact information for individuals to file complaints or inquire about employment classification status. The posting must appear in both English and Spanish and/or other languages as appropriate and must be constructed of materials capable of withstanding adverse weather conditions. The notice will be created by the Commissioner of Labor and will be available on the New York State Department of Labor's website (http://www.labor.ny.gov) within thirty (30) days of the Act's effective date. Failure to comply with these notice and posting requirements can result in civil penalties totaling up to $2,500.

Violations and Penalties

Civil penalties for violations of the Act are $1,500 for a first violation and up to $5,000 for subsequent violations within a five-year period. In addition, any contractor who "willfully" fails to properly classify a construction worker as an employee will be subject to both criminal and civil penalties under the Act. A "willful violation" occurs if the contractor "knew or should have known that his or her conduct was prohibited" under the provisions of the Act. Where a "willful violation" is found, civil penalties range from $2,500 per misclassified employee for a first offense to $5,000 for each misclassified employee for each subsequent offense within five years. Contractors who willfully misclassify construction workers can also be charged with a misdemeanor and, upon conviction, shall be subject to imprisonment for not more than 30 days or a fine not to exceed $25,000 for a first offense, which fines in the case of a subsequent offense can extend up to $50,000 or *imprisonment* for not more than 60 days.

As with other labor laws prohibiting the misclassification of workers as independent contractors, the Act contemplates potential individual liability as well. Accordingly, where the contractor is a corporation, any officer or shareholder who owns or controls at least 10 percent of the outstanding stock, “who knowingly permits” the corporation to willfully violate” the law, is also subject to civil and criminal penalties. In the event of a criminal conviction, the Act also provides for debarment from public works contracts for one to five years. Finally, any contractor subject to civil penalties under the Act is also subject to the array of remedies and penalties available under other laws, including business, corporate or personal income tax liability, as well as penalties arising under the New York State Unemployment Insurance and Workers’ Compensation Laws.

Retaliation

The Act prohibits employers from retaliating against any employee for exercising any rights granted under the Act, including, but not limited to, making complaints to an employer or causing any proceeding to be initiated under the Act. Any employer who engages in retaliatory actions can be subjected to the criminal and civil penalties described above.

What Employers Need to Know

If signed into law by the Governor, the Act will redefine how construction workers are classified. Steep penalties flow from the misclassification of workers and, therefore, prudent employers should be careful in classifying workers as independent contractors. Where uncertainty exists as to the worker's proper classification, seeking legal guidance is a good idea given the potential penalties under the law.

As previously discussed at Proskauer's breakfast seminar in late March [*Misclassification of Workers*], our webinar on May 26, 2010, and in article [*Misclassifying Workers As Independent Contractors: Risky Practice, Costly Mistake*], employers act at their peril for misclassifying workers as independent contractors. The New York State Construction Industry Fair Play Act is only the latest effort by New York State to "root out" business behavior that deprives the State of needed tax revenues and "creates an unlevel playing field for law-abiding employers." In addition, as was made clear at a recent "stakeholders" meeting at the U.S. Department of Labor, the construction industry is also being targeted at the federal level for widespread use of independent contractors which has given rise to the view that substantial misclassification exists in the industry.

We will keep you posted as to when the Act is signed into law. In the meantime, if you have any questions about this client alert, or the manner in which your business has classified employees, please contact your Proskauer relationship lawyer or any of the Co?Chairs of Proskauer's Employment Law Counseling Practice Group.

*Special thanks to associate **Latoya Moore** for her assistance in drafting this Client Alert.*

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