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Redefining "Employee" in Ohio

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In recent months, there has been increased scrutiny by state and federal regulatory agencies of independent contractor relationships. An agency finding that an employer has misclassified an individual as an independent contractor (versus an employee) is an expensive proposition for an employer – and a revenue boost to various agencies who receive thousands of dollars in past and future unemployment premiums, payroll taxes and workers' compensation premiums. Currently, a 20 factor test developed by the IRS is most frequently used to determine whether an independent contractor is truly "independent" and not an employee. Ohio legislators currently are deciding whether Ohio should have its own, more expansive, definition of "employee."

On May 25, 2010, H.B. 523 was introduced in the Ohio General Assembly proposing a uniform definition of employee for purposes of the Ohio laws governing:

1. the payment of minimum wage;
2. the payment of prevailing wages;
3. workers' compensation;
4. unemployment compensation; and
5. state income taxes.

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Under current Ohio law, each statute includes its own definition of employee. The proposal also provides a seven-part test to determine whether an individual qualifies as an independent contractor, prohibits misclassification of employees and retaliatory actions by employers, addresses complaint filing and investigation procedures and imposes penalties against employers for violations.

The proposal broadly defines employee as "an individual who performs services for compensation for an employer." The proposal also eliminates the requirement that due consideration and great weight be given to the definition of employee under the Fair Labor Standards Act (FLSA). Therefore, Ohio's definition of employee could lead to results that are inconsistent with FLSA interpretations. The proposed seven-part independent contractor test is similar to the 20-part test used by the IRS (e.g. who controls the work, who retains liability for business expenses, whether the parties have entered into a written independent contractor agreement). The final test in the proposal, however, could lead to many current independent contractors becoming employees. The final test is whether "[t]he service performed by the individual is outside of the usual course of business for the employer." Many employers, for a variety of reasons, outsource some of their normal business activities to independent contractors. Under H.B. 523, these contractors could quite possibly fall under the new employee definition.

The proposal contains a complaint process and, as found in most employment-related statutes, an anti-retaliation provision. The proposal prohibits employers from obtaining waivers from individuals or entering into agreements that would result in the misclassification of the individual. Under the proposal, the director of commerce is empowered to issue cease and desist orders; collect any wages, salary, employment benefits, or other compensation denied or lost to an individual due to the misclassification; and assess civil penalties of up to $1,500 ($2,500 for each repeat violation). "Willful violations" may result in punitive damages as well as criminal penalties.

Ohio employers should keep a close eye on H.B. 523, as well as an Ohio Senate proposal addressing the same issue (S.B. 195) and, in the meantime, conduct a self-audit of current independent contractor relationships. Competent employment counsel should be consulted to develop a plan to address this issue in the event H.B. 523, or similar legislation, becomes law.

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