

The Illinois Employee Classification Act

By: Lawrence L. Pratt, Member

The Illinois Employee Classification Act went into effect on January 1, 2008 and represents a dramatic shift in Illinois law regarding independent contractors. The act deals ostensibly with the construction industry, but as we often see, the devil is in the details. The Act can apply to everyone from interior decorators to trucking firms - entities not normally considered in the construction industry. It changes the rules by which workers are considered employees versus independent contractors and provides stiff civil and criminal penalties for those entities that get it wrong.

Section 10 of the act attempts to clarify to whom this law applies. According to subsection (a), an individual performing services for a contractor is automatically deemed an employee unless certain exceptions contained in subsections (b) and (c) apply. The next question is who is a "contractor"?

Section 5 defines a contractor as "... any sole proprietor, partnership, firm, corporation, limited liability company, association or other legal entity permitted by law to do business with the state of Illinois who engages in construction as defined in this Act."

Now it gets interesting. Under the Act, "construction" means:

...any construction, altering, reconstructing, repairing, rehabilitating, refinishing, refurbishing, remodeling, remediating, renovating, custom painting, decorating, demolishing, and adding to or subtracting from any building, structure, highway, roadway, street, bridge, alley, sewer, ditch, sewage disposal plant, water works, parking facility, railroad, excavation or other structure, project, development, real property or improvement, or to do any part thereof, whether or not the performance of the work herein described involves the addition to, or fabrication into, any structure, project, development, real property or improvement herein described of any material or article of merchandise. Construction shall also include moving construction related materials on the job site to or from the job site.

All clear? Right.... The two main effects of this Act are first, to create a new presumption that a

worker is an employee; and second, to cast a broad net encompassing many more businesses and trades than normally considered part of the construction industry.

To understand how to interpret this Act, and more importantly how it will be enforced, it is helpful to look at where the idea of the Act originated. The Act's primary purpose is to address the issue of misclassification of workers in Illinois. The supporters of the Act believed, correctly or not, that thousands of workers in Illinois were being misclassified as independent contractors when they were really employees. Why is the State of Illinois so concerned about this problem? Simply, tax revenue.

According to a December 2006 study conducted by the University of Missouri- Kansas City the State of Illinois lost an estimated \$124.7 million in income tax revenue annually between the years 2001 and 2005 alone, \$8.9 million of that in the construction sector. The study also concluded that there was a 55 percent increase in the number of misclassified workers during the same period. As a result of misclassification, the study reported that workers were underpaid by \$23 million during the period.

It comes as no surprise that the Act's primary sponsors were the AFL-CIO, Laborers' International Union, and Foundation for Fair Contractors. This is why, even though the construction industry represented only a fraction of the misclassifications, the Act focuses on construction.

These organizations argued to legislators that independent contractors do not receive workers' compensation benefits, do not have taxes withheld for them and do not have unemployment benefits paid in for them but are being paid a wage just like an employee.

So where does this leave us? The Act does not do away with the independent contractor relationship altogether. If the "individual providing services" meets the following requirements of the Section 10 (b) Act he/she will be deemed an independent contractor:

1. If the individual is free from control over the performance of the job;
2. The work is outside the usual course of services performed by the contractor; and
3. The individual is engaged in an independently established trade.

4. The individual is deemed a legitimate sole proprietor or partnership under subsection (c) of this section.

Number 4 is of particular interest because even if a worker does not fit into numbers 1 through 3, he/she can still qualify as an independent contractor under subsection (c). However, subsection (c) sets forth a dozen criteria that must be met:

1. Perform the service free from the direction or control of the contractor;
2. Not be subject to dissolution upon severance of the relationship;
3. Maintain a substantial investment of capital in the business;
4. Own the capital goods and gain the profits of the business;
5. Make its services available to the general public on a continuing basis;
6. Include services rendered on a federal income tax schedule as a business;
7. Perform services for the contractor under the name of the business;
8. Obtain and pay for any necessary licenses in the name of the business;
9. Furnish the equipment necessary to provide the service;
10. Hire its own employees without contractor approval, pay them without reimbursement from the contractor, and report income to the IRS;

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A Change in Missouri Law Means More Discrimination Cases Will Be Going To Trial

By: John A. Michener, Member, and Talmage E. Newton IV, Associate

Employment Discrimination Overview

With the exception of unionized and contractual employees, the vast majority of today's workforce is made up of "at will" employees. As many employers know, an "at will" employee can be fired for any reason – or for no reason. A caveat on this practice is that they may not be fired for an illegal reason.

Illegal reasons for termination are defined by a variety of sources, including federal statutes such as Title VII of the Civil Rights Act of 1964, state discrimination statutes such as the Missouri Human Rights Act, and local and municipal ordinances. While these "illegal reasons" vary from state to state – and even within various counties inside states – there is a national obligation to provide equal employment opportunity to employees without regard to age, sex, pregnancy, race, color, national origin, religion, disability or military status. It is within these specifically enumerated categories that the majority of terminated employees seek redress after termination.

Previous Missouri Standard

Until recently, to prevail upon a discrimination claim in Missouri courts, a plaintiff would have to allege he was a member of a statutorily protected category and that he had been terminated or otherwise discriminated against because of his membership in that protected class. The employer could then respond with a legitimate nondiscriminatory reason for the termination (e.g., poor performance, habitual tardiness, etc). The burden then shifted back to the plaintiff to prove the legitimate reason proposed by the employer was just a pretext to cover the discrimination.

Under the previous standard, an ex-employee suing in Missouri courts was required to prove that the discrimination she alleged existed and that it was a *motivating or determining* factor in her termination. (Note: This is still the standard in Missouri's federal courts). This standard put a very high burden of proof on the terminated employee. It meant that even with the existence of discriminatory behavior, if the employer

could point to a legitimate reason, they were more likely to prevail on summary judgment and avoid trial.

More State Discrimination Cases Headed for Trial in Missouri

In 2007's *Daugherty v. City of Maryland Heights*, the Missouri Supreme Court changed the state standard in summary judgment motions and held that for a plaintiff/employee to survive summary judgment and move on to trial, he only needed to prove that the alleged discrimination was a "contributing factor" in his termination. This decision is in contrast with the much higher federal standard of "motivating or determining."



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This relaxed standard means that plaintiffs do not need to establish discrimination as the motivating factor of their termination. For all intents and purposes, to get their claims before a jury, ex-employees now only need to establish that they were subjected to discrimination.

Protecting Your Company

Given the increased likelihood of employment discrimination cases making it to trial in Missouri courts, it is even more important that employers protect themselves. There are a number of ways to do this. The most obvious is by having policies in place that prohibit this type of discrimination. These policies include both mission statements prohibiting discrimination, as well as widely distributed employment manuals. Employers must communicate these policies to their workers and set up a frame through which employees are made aware of the policies and violations that can be easily reported. (TIP: Employers may want to require employees to sign a form acknowledging they have reviewed the employment manual and will abide by its contents. More specifically, employers may want to have employees sign nondiscrimination agreements).

Equally important to setting up clear policies is enforcing them when they are violated. As we all know, policies without enforcement appear hollow and could subject a company to more damages than if there were no policies at all. Offending employees must be subjected to counseling and/or discipline.

In addition to establishing policies prohibiting discrimination, it is equally important for employers to keep detailed and accurate records on the performance of their employees. A discrimination claim can be more easily defended by a detailed employment record that shows a legitimate reason for termination. A jury will want to know if an employee missed 20 days of work last month, whether they were underperforming, missing deadlines or not hitting quotas. In the absence of this documentary evidence, a jury may instead be led to believe that the company is "making up" the poor performance to mask a discriminatory termination. Such a result could leave employers vulnerable to hefty jury awards for back wages, punitive damages and even the former employee's attorney's fees.

With some simple steps, a company will be able to both prevent discrimination within its workplaces and do more to overturn false claims of discrimination by disgruntled ex-employees. ■

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11. Not be held out by the contractor to the public as its own employee; and
12. Have the right to perform similar services for others.

If the worker does not meet any one of these then he/she will be considered an employee.

So what can be done short of considering all formerly independent contractors as employees? According to the rules recently laid down by the

Illinois Department of Labor, incorporation of independent contractors may be one answer. If all of your subcontractors are corporations then they will qualify as independent contractors under Section 10 (a). The challenge is going to be in making sure the subcontractors a contractor is dealing with really are bona fide corporations. The Department may look at factors such as whether the corporation is capitalized, whether it has issued stock, whether there is a separate corporate account, and whether the corporation

maintains separate books and minutes of meetings. At a minimum, this means checking on whether the independent contractor has Articles of Incorporation on file with the Department of Revenue and that they remain in good standing during the course of the contract. To be safe, all standard subcontractor agreements should be reviewed to determine if they do meet the requirements set out in Section 10 (a) and make changes where necessary. ■

The Illinois Employee Classification Act Part II: Enforcement

By: Lawrence L. Pratt, Member

The Illinois Employee Classification Act mandates that the Illinois Department of Labor shall be empowered to enforce the Act. The department has full investigatory powers, including subpoena power to compel testimony and for the production of documents. The Act also gives the department the power to issue Cease and Desist Orders, file suit for contempt, collect wages due, and assess a civil penalty of \$1,500 for the first offense and \$2,500 for each successive violation. Each day the condition persists is considered a separate violation under the Act.

If the offense is considered willful and wanton then the fines are doubled and the first offense is considered a Class C misdemeanor. For subsequent offenses within a 5-year period a contractor can be charged with a Class 4 felony. Further, any contractor that infringes on the Act more than once will suffer what the Act refers to as “disbarment”. Disbarment is a prohibition against that contractor from bidding on state contracts for a period of 4 years.

Most significantly, the Act compels the Department of Labor to cooperate and share information with the Department of Employment Security, the Department of Revenue, and the Workers’ Compensation Commission. A finding of worker misclassification by the department against a contractor can quickly cascade into investigations and charges of non-compliance from these other state agencies as well.

The Act also provides for a private right of action for back wages and benefits, compensatory damages of \$500 for each violation, and for unlawful retaliation, equitable relief and attorney’s fees.

An interesting aspect of this Act worth noting, and one that clearly indicates its origins, is Section 25-Enforcement. It appears that not only may an aggrieved party file a civil claim and make a complaint to the Department of Labor, but “any interested party” may also. Not only can a third-party make the complaint, that third-party can receive up to 10% of

the spoils collected by the Department. In criminal circles we call this “bounty hunting”. This is one way to change the balance of power at the negotiating table when the collective bargaining agreements come up for renewal.

This Act may represent a trend nationwide. New Jersey, Massachusetts, and New Mexico have passed similar acts and New York has intensified its enforcement efforts in these areas. Be advised, the federal government has taken notice. Last year the Independent Contractor Proper Classification Act of 2007 (ICPCA) was introduced in the Senate. This bill has much of the same characteristics as the Illinois Employee Classification Act. Only time will tell how far this trend will continue. ■

Homeowner’s Insurers Operating in the State of Missouri Are Not Affording Themselves Maximum Protection

By: David W. Cooper and Ellen J. Brooke, Attorneys

According to a report issued by Midwestern Governors’ Association, “In 1995, the Missouri State Highway Patrol witnessed a 470 percent increase in methamphetamine lab seizures in the State of Missouri.”¹ On June 15, 2005, Governor Matt Blunt signed into law restrictions on the sale of pseudoephedrine (PSE) products. The law places products under Schedule V requirements, which requires them to be placed behind the pharmacy counter, and they can only be dispensed by a pharmacy or a pharmacy technician. *Id.* at Page 1.

The manufacture of methamphetamine is simple because it does not require agriculture, specialized equipment, or advanced technical training. It is essentially “cooked” by anyone in a make shift lab hidden in mobile homes, warehouses, or even motel rooms. Congress enacted the Methamphetamine Control Act of 1996 to curb the production of abuse of methamphetamine by controlling the key chemicals necessary to produce the drug and by increasing criminal sentences for possession and distribution.² Production and distribution remain high nonetheless.

Most homeowner’s insurers operating in the State of Missouri issue homeowner’s policies based upon ISO standardized forms. Since 1971, ISO has been a leading source of information about risk. The company provides data, analytics, and decision-support services for professionals in many fields, including property and casualty insurance.³

The standard ISO homeowners policy contains the

following intentional acts exclusion:

SECTION I – EXCLUSIONS

WE DO NOT COVER LOSS RESULTING DIRECTLY OR INDIRECTLY FROM:

8. INTENTIONAL LOSS, MEANING ANY LOSS ARISING OUT OF ANY ACT COMMITTED:

- (1) BY OR AT THE DIRECTION OF AN INSURED; and
- (2) WITH THE INTENT TO CAUSE A LOSS.

Under such an exclusion, consider the following circumstances:

- a. An insured moves into a home. He or she obtains homeowner’s insurance, and then sets up a methamphetamine laboratory. During the process of producing methamphetamine, the insured “accidentally” starts a fire and burns the home down;
- b. An insured is selling methamphetamine or related drugs from his or her residence premises. After a period of time, there is a burglary at the residence premises resulting in damage or loss. It is evident from the condition of the property following the burglary that the thieves were looking for drugs or proceeds from drug sales.

Under each of these scenarios, the above-referenced claims would be covered as “accidental losses” incurred by the insured

without any intentional conduct on their behalf. There are, however, different provisions and exclusions in homeowner’s policies approved for use by the Missouri Department of Insurance that would not allow for recovery on the same facts, including the following:

Losses We Do Not Cover Under Coverages A and B

We do not cover any loss to the property described in Coverage A – Dwelling Protection or Coverage B – Other Structures Protection, consisting of or caused by:

8. Any substantial change or increase in hazard, if changed or increased by any means within the control or knowledge of an insured person.
9. Intentional or criminal acts of or at the direction of any insured person, if the loss that occurs:
 - (a) May be reasonably expected to result from such acts; or
 - (b) Is the intended result of such acts.

This exclusion applies regardless of whether or not the insured person is actually charged with, or convicted of a crime.

As noted, both of these exclusions have been approved by the Missouri Department of Insurance and are regularly enforced. Should a carrier wish to protect itself against the hazards of methamphetamine manufacturing and/or sale, these exclusions should be included in the standard homeowner’s policy exclusions, as opposed to relying upon the ISO standard forms. ■

Footnotes:

1. Indiana Criminal Justice Institute on behalf of the Midwestern Governors’ Association Regional Methamphetamine Summit, December, 2005.

2. Methamphetamine in Missouri, a Missouri Division of Alcohol and Drug Abuse Policy Brief, James Topolski, Ph.D. and Karen Kadela, “Methamphetamine in Missouri”.

3. HYPERLINK “<http://www.iso.com>” <http://www.iso.com>.



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Best regards,

James E. Godfrey, Jr.
Civil Litigation Practice Group Leader

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