

NEW MN CONSTRUCTION WORKER LAWS: UNDERSTANDING EMPLOYEE MISCLASSIFICATION
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EMPLOYMENT VS. INDEPENDENT CONTRACTOR

- It is common practice in your industry to call workers independent contractors
- Save money on payroll taxes, workers compensation, etc.
- Eliminates other employer duties and responsibilities towards worker
- Rule of thumb: Construction personnel are employees, and it can be very hard to prove otherwise





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EMPLOYMENT VS. INDEPENDENT CONTRACTOR

- The general rule is that anyone who performs services for you is your employee if you can control what will be done and how it will be done.
- You can still exercise broad control over the jobs an independent contractor performs but cannot control the specific means or way the jobs are performed.
- A classic example is the plumber you hire to come fix a leaky pipe in your house. You "control" the plumber by pointing him to the leaky pipe and asking him to fix it, but he performs the work with his own tools, in the manner he sees fit.

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TRADITIONAL LEGAL TEST

- To qualify as an independent contractor in general the hired party must:
 - Have the right to control the means and manner of performance
 - Be paid on a percentage or per job basis
 - Furnish its own tools and materials
 - Have control over how the work is done



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CONSTRUCTION CONTRACTOR TEST

- The law gives additional direction to subcontractors in the construction industry on this issue.
- A new 14-factor test will replace the existing 9-factor test on March 1, 2025.
- There are now more specific rules regarding the independent contractor's business registration, tax reporting, and contract language.
- New penalties can also be imposed by the state.



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EMPLOYMENT VS. INDEPENDENT CONTRACTOR TEST

- The default rule is that a construction worker is an employee unless proven otherwise.
- Effective March 1, 2025, an individual providing or performing commercial or residential building construction or improvement services is an independent contractor only if the individual operates as a business entity that meets all 14 requirements when services are provided or performed.
- **Yellow highlighted items below are new under the 14-point test**

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INDEPENDENT BUSINESSES?

- **Must operate as a business entity**
- **Must be established and maintained separately from and independently of the party whom the services were provided or performed**
- Key point is that this is a business arrangement between two legitimately separate companies



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REGISTERED AS A BUSINESS ENTITY WITH THE STATE

- **Is in good standing with the Minnesota Secretary of State**
- Important to maintain that standing - something that can be easily checked on the Secretary of State's website



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OTHER STATE LAW COMPLIANCE REQUIREMENTS

1. Has a Minnesota unemployment insurance account if required;
2. Has obtained required workers' compensation insurance coverage if required;
3. Is registered as a construction contractor with the Minnesota Department of Labor (or and holds license if applicable, such as a residential building contractor license;



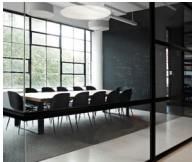
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FORMAL TAX REQUIREMENTS

- Subcontractor must comply with all of the following:
 - (i) holds a federal employer identification number if required by federal law;
 - (ii) holds a Minnesota tax identification number if required by Minnesota law;
 - (iii) has received and retained 1099 forms for income received for building construction or improvement services provided or performed, if required by Minnesota or federal law;
 - (iv) has filed business or self-employment income tax returns in the previous 12 months, including estimated tax filings, with the federal Internal Revenue Service and the Department of Revenue, as the business entity or as a self-employed individual reporting income earned, for providing or performing building construction or improvement services, if any; and
 - (v) has completed and provided a W-9 to the party for whom the services were provided or performed if required by federal law.




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CONTRACTOR USES ITS OWN EQUIPMENT

- Owns, rents, or leases equipment, tools, vehicles, materials, supplies, office space, or other facilities that are used by the business entity to provide or perform building construction or improvement services
- Leases from the general contractor are fine, if they are legitimate and well-documented




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NON-EXCLUSIVITY

- Provides or performs, or offers to provide or perform, the same or similar building construction or improvement services **for multiple persons or the general public.**
- In other words, the subcontractor should not provide services exclusively to a single general contractor.



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FORMAL WRITTEN CONTRACT REQUIREMENT

- Subcontractor must be operating under a written contract that:
 - (i) is signed and dated by both parties;
 - (ii) **is fully signed no later than 30 days after the date work commences;**

*Does not apply to change orders.

 - (i) identifies the specific services to be provided or performed under the contract;
 - (ii) **States the subcontractor controls the means of providing the services;** and
 - (iii) provides for compensation on a commission or per-job or competitive bid basis and not on any other basis.
***NO HOURLY WORKERS**




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INVOICE AND NON-CASH PAYMENTS REQUIRED

- Submits invoices and receives payments in the name of its business entity.
- **Payment in cash not allowed**




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SUBCONTRACTOR MUST CONTROL THE MEANS OF PERFORMANCE

- The business entity actually controls the means of providing or performing the specific services
- This issue of control is at the heart of the traditional analysis



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SUBCONTRACTOR MUST BEAR ITS OWN EXPENSES

- The subcontractor must incur the main expenses and costs related to providing or performing the specific services under the written proposal, contract, or change order.
 - **Can the GC buy the materials?**
- Consistent with the broader need for the subcontractor to be a legitimate, separate business

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SUBCONTRACTOR RESPONSIBLE FOR BUSINESS FAILURES

- Subcontractor is responsible for the completion of the specific services and for failure to complete the specific services.
 - Can they profit or lose based on how long it takes to do the work and if they must correct or replace the work?
- This business risk cannot simply be passed along to the general contractor, as would generally be the case with an employee.

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CAN THE SUBCONTRACTOR GO OUT OF BUSINESS?

- Subcontractor may realize additional profit or suffer a loss if their time and costs exceed the agreed upon price.
- Again, the key question is whether the subcontractor, like all legitimate businesses, actually faces business risk.




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EMPLOYEE VS. INDEPENDENT CONTRACTOR

- Why does the distinction matter?
 - **In a word, taxes.**
- Both the State and Federal Governments have a strong interest in collection all the taxes that must be paid by employees and employers are part of an employment relationship.
- These taxes fund many programs designed to protect employees, including unemployment insurance and worker's compensation.



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HEIGHTENED LEGAL CONSEQUENCES

- **What's the worst that could happen if you misclassify?**
- The IRS and the Minnesota Department of Revenue, and Minnesota Unemployment Department can seek to recover unpaid withholdings from owners personally.
- Claims by the "employees":
 - Unpaid overtime
 - Minimum wage
 - PTO / vacation time
 - Paid save and sick leave.
- Possible criminal investigation?
- Nightmare scenario is a worker's compensation claim filed after a worksite injury.
 - Could easily give rise to seven-figure potential liability.
 - Risk can be minimized by sound classification practices, forcing your subcontractors to carry their own worker's compensation insurance, and/or obtaining "if any" coverage from their insurer.


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MISCLASSIFICATION PENALTIES

- Penalties of up to **\$10,000 each time** a person is misclassified under the 14-factor test, or for each employee they require to register as a construction contractor.
- Construction contractor owners, officers, or agents who knowingly or repeatedly engage in any of the prohibited activities may be held **individually liable**.



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BROAD GENERAL CONTRACTOR LIABILITY

- Under the new law, upstream general contractors also face increased liability for misclassifying workers.
- If a subcontractor fails to meet each of the 14 factors at a time the services were provided:
 - all its employees will be considered employees of the hiring party.
 - the hiring party will be liable for all misclassifications, i.e. penalties.




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STOP ORDERS

- As of March 1, 2025, DOLI will have significantly enhanced enforcement powers, including the issuance of stop orders in the construction industry.
- With a stop order, DOLI may order a business to cease operating at one or more of its workplaces if DOLI determines the business violated one or more laws, including those related to misclassification.
- The stop order will remain in existence until the Commissioner lifts it upon finding the business has come into compliance with applicable law and paid any damages and penalties.
- Could become an extremely powerful tool for regulators.



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QUESTIONS?

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