

The Legal Review

A Monthly Email Newsletter to Analyze and Share Case Law Precedent that Affects Our Industry

A Complimentary Resource from
Breedlove & Associates

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Introducing *The Legal Review*. In an effort to help our agency partners strengthen their business practices and steer clear of legal trouble, we will share findings from relevant legal cases. We've found that the easiest way to gain a practical understanding of complex tax and labor law is by reviewing real-life situations. These stories will illuminate potential legal landmines for your agency and/or your clients, and more importantly, show you how to avoid them.

Misclassifying Temporary Nannies: The State of Oregon Department of Labor vs. A Nanny Placement Agency.

The Mistake

The Agency termed their temporary nannies "independent contractors." The Agency had produced and provided written materials (website, marketing materials, etc.) stating that the temporary nannies they placed were independent contractors. Why did they do this? Their intention was to eliminate any potential liability as the employer of their temporary nannies. Calling them independent contractors seemed like a simple – and harmless – way of absolving themselves of the responsibilities that come with being an employer.

The Law

Why is this a problem? A nanny is never an independent contractor; she is classified as the employee of the family she works for. Even though it happened unknowingly, the Agency had directly contradicted the law by classifying their temporary nannies as independent contractors. In legal terms, these are very different employment concepts.

You may be asking, "so what?" The state and federal tax agencies view this as a serious issue because:

- a) worker can be classified as an independent contractor only if they have control over all aspects of the work environment and take direction from no one. Otherwise, they are classified as an employee; and
- b) the government wants their tax dollars – independent contractors pay both the employer and the employee payroll taxes whereas employees & employers each pay a portion of the taxes. Some employers misclassify employees intentionally in order to avoid payroll tax responsibilities.

The Mess

- One of the frequently-placed temporary nannies found herself temporarily out of work and filed for unemployment benefits. When asked about her previous employers, she listed the Agency.
- The Agency received a statement from the Oregon Department of Labor informing them of the unemployment benefits claim from the temporary nanny. The Agency responded in writing indicating that the temporary nanny was not their employee, but rather the employee of the families for whom she worked.
- The State viewed this as highly suspicious and decided that a full audit was warranted. The State felt that the Agency was guilty of tax evasion by misclassifying their employees as independent contractors.

Note: Payroll tax evasion by misclassifying employees as independent contractors is widespread and a "hot button" for state tax agencies.

Note: The fact that the families are the employers was not introduced into the audit initially. The sole focus was on the Agency's illegal practice of calling nannies independent contractors.

The Mess (continued)

- The State reviewed files, fee structure, placement process, etc. They also conducted interviews with the agency and temporary nannies.
- The Agency was forced to retain a lawyer to defend itself from charges of tax evasion.
- The Agency also solicited the assistance of Breedlove & Associates as an industry expert.
- A deposition was held to discuss the findings and to formulate a ruling. Parties in attendance included: Owner of the Agency, the Agency's lawyer, a state auditor, the state comptroller, and Stephanie Breedlove (via conference call).

The State's Position: Temporary nannies are not independent contractors; they are the employees of the Agency. The Agency is not in compliance with the law and is, therefore, subject to back taxes, penalties and interest. Effective immediately, the Agency will also need to restructure its temporary placement business to treat temporary nannies as employees of the agency.

The Agency's Position: The Agency agreed that temporary nannies are not independent contractors and admitted that they had mistakenly misclassified the nannies. The Agency then built a case that temporary nannies are employees of the families they work for – and came to the meeting with restructured documents that corrected the inadvertent misclassifications. Breedlove & Associates presented a formal verbal and written case using IRS Publication 926, the Fair Labor Standards Act and the Independent Contractor 20 Point Test to provide legal support for the assertion that temporary nannies placed by the Agency are in fact employees of the families they work for. The Agency also committed to providing the Breedlove & Associates educational literature on Tax Law for Temporary Employment as a means of informing both clients and nannies on their tax responsibilities. Finally, the Agency stated that if the State enforced its tax evasion charge (and the corresponding financial penalties), the Agency would be forced to close its doors.

The Outcome

After additional review and interviews, the State accepted the Agency's position and proposed business practice changes. WHEW! Unfortunately, even in "victory," the State audit had taken its toll on the Agency in the form of several months of lost productivity and stress as well as hefty legal bills from its attorney.

How The Whole Thing Could Have Been Avoided

In this case, there are two simple ways to eliminate this legal risk:

1. The Agency should have classified temporary nannies according to the law – as employees of the families they work for.
2. The Agency should have informed clients and nannies that temporary nannies are classified as employees of the families they work for. By including this information in their placement process, they may have prevented the unemployment claim against them that kicked off the entire case!

If you have additional questions, please visit www.breedlove-online.com or call us toll free at 888-BREEDLOVE (273-3356). We're here to help our agency partners provide their candidates and clients with information, tools and resources that improve the employment relationship, eliminate legal risk for all parties, and generally increase the professionalism of the industry.

