Advisory

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Connecticut Supreme Court Confirms that Independent Contractors are not "Misclassified" Employees Simply Because They Only Work for One Company

In a welcome development for Connecticut companies that routinely rely on consultants, the Connecticut Supreme Court ruled in Southwest Appraisal Group LLC v. Administrator, Unemployment Compensation Act that individuals can still be properly classified as independent contractors even if they work exclusively for one entity. The decision was released on March 21, 2017.

Southwest Appraisal Group ("Southwest") is in the business of assessing damaged vehicles. Insurance companies contract with Southwest to perform these inspections, which Southwest subcontracts out to individual appraisers. Following a routine tax audit, the Unemployment Compensation Act Administrator concluded that Southwest had misclassified certain appraisers as independent contractors when they should have been designated as employees, and thereby owed thousands of dollars in unemployment contribution taxes. Southwest challenged the decision but the trial court sided with the Administrator as to those appraisers who did not work for anyone other than Southwest. The Connecticut Supreme Court reversed, holding that "a putative employee's work for other entities is a relevant, but not dispositive, factor" in a misclassification analysis.

Under Connecticut law, the "ABC Test" determines whether an employment relationship exists for purposes of the Unemployment Compensation Act (the "Act"). In order to be an independent contractor, all three prongs of the ABC Test must be met, namely: (A) the individual is free from direction and control when performing his/her services; (B) the services are performed outside the usual course of the company's business or outside all the company's places of business; and (C) the individual "is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service performed." Unless all three prongs of the ABC Test are satisfied, an employment relationship will be found.

While acknowledging that the Act "should be liberally construed in favor of its beneficiaries," the Court warned that it "should not be construed unrealistically in order to distort its purpose." Indeed, "it is important to consider that the [independent contractor] exemption becomes meaningless if it does not exempt anything from the statutory provisions." Thus, in applying the ABC Test, the Court "must balance preventing the use of sham independent contractor agreements to avoid unemployment insurance obligations against 'hampering those who undertake to do business together as independent contracting parties, rather than as employer and employee,' on a legitimate basis." To

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strike this balance, one must assess the totality of the circumstances under Part C by accounting for numerous factors, including:

1. The existence of state licensure or specialized skills;
2. Whether the individual holds him/herself out as an independent business through business cards, printed invoices or advertising;
3. Whether the individual has a place of business separate from the potential employer;
4. The individual's capital investment in his/her independent business;
5. If the individual has his/her own liability insurance;
6. If the individual performs services under his/her own name or the employer's name;
7. If the individual employs or subcontracts others;
8. If the individual has a saleable business with established clientele;
9. Whether the individual performs services for more than one entity; and
10. Whether the performance of services affects the goodwill of the individual rather than the putative employer.

The existence of some or all of these factors can be used to satisfy Part C of the ABC Test, but no single factor is dispositive. "Giving improper primacy to [an individual's work for other entities] risks 'subjecting an employer unfairly to the decisions of the putative employee and an unpredictable hindsight review,' without consideration of 'the intent of the parties, the number of weekly hours the putative employee actually worked for the employer, or whether the putative employee even sought other work in the field." It would also "have a chilling effect on businesses' willingness to contract with otherwise legitimate small businesses with minimal client bases and revenues, such as those run as start-ups or by persons who are transitioning to retirement." Thus, the Court held that performing services for multiple clients is not a prerequisite to meeting Part C of the ABC Test.

The Connecticut Supreme Court's decision proves that the State does not intend to make the defense of an "independent contractor" classification any harder than it already is. Companies that hire independent contractors will nevertheless remain under the microscope and should be prepared to prove each element of the ABC Test, if necessary. In conducting a Part C analysis, it is imperative that all of the factors enumerated by the Court in Southwest be taken into account. Businesses should bear in mind the Connecticut Supreme Court's cautionary note that, although not a litmus test, "evidence of the provision of services to third parties, or lack thereof, becomes more significant in proving independent contractor status in the context of cases lacking other indicia of a putative employee's independent enterprise."