What is Employee Misclassification and why does it matter?

There are multiple aspects to the issue of misclassification, and the issue affects employers and employees throughout New Hampshire, New England and countrywide. **Correct classification of workers has important implications with regard to labor standards such as minimum wage and overtime requirements, unemployment insurance, federal and state payroll taxes, business profits taxes, compliance with workplace safety and health requirements and workers' compensation insurance.**

Several types of misclassification exist. Within the arena of workers' compensation insurance, workers are classified by the type of work they actually do, and workers' compensation rates depend on that classification. Workers' compensation insurance for a clerical worker will cost much less than workers' compensation insurance for a drywaller or a logger. If an employer misrepresents or otherwise misinforms its insurer about what type of work their workers are actually doing, the insurance premium will be incorrect for the exposure. While this would likely get adjusted eventually, it certainly has an effect on the cost of doing business for the employer and may affect its competitive position in their marketplace - and the result is that honest employers who correctly represent their workers may end up paying more than their fair share.

In addition to this type of misclassification there is also the issue of the underground economy. In some cases workers are paid in cash for work they do and never appear on the books and in the records of any employer. They aren't so much misclassified as not classified at all since there is no documentation of their work status. The same issues of workers' protections and benefits that are mentioned above obviously apply to workers who are part of the underground economy.

Perhaps the most high profile misclassification issue here in New Hampshire is the determination as to when someone can qualify as an independent contractor under the set of criteria that New Hampshire uses. For Department of Labor/Workers' Compensation purposes, an entity or individual must meet all of the criteria listed under **NH RSA 281-A:2 VI(b)** in order to be considered an independent contractor. If they fail to meet even one of the criteria they can not qualify as an independent contractor and are subject to the requirements of the law, as is anyone who hires them. NH Employment Security and the Department of Revenue Administration have their own tests for determining employment, and these determinations affect, among other things, unemployment insurance and the correct payment of business taxes.

**For those who qualify as independent contractors, it is their choice whether or not to cover themselves for Workers' Compensation. In any case where they have chosen not to, the independent contractor may be assuming that other insurance they carry, such as health insurance, disability insurance or even automobile insurance, will provide them coverage in the event of injury. This may very well not be the case. Most, if not all, automobile and disability policies exclude coverage for occupational injury (i.e. injury sustained while working), as do many health insurance policies. Anyone making the legal choice not to have Workers' Compensation coverage should check with their other insurance companies and/or their producer (agent or broker) for more information.**

For more information on Employee Misclassification, please visit [www.nh.gov/nhworkers](http://www.nh.gov/nhworkers).
Under New Hampshire Unemployment Tax Law, most employers are liable to pay unemployment taxes and report wages paid to their employees on a quarterly basis. Employers must complete an employer status report within 30 days of first furnishing employment in New Hampshire. [http://www.nh.gov/nhes/employer/documents/empstatus.pdf](http://www.nh.gov/nhes/employer/documents/empstatus.pdf) Upon receipt of the completed form, a determination of liability will be made and the employer will be notified. Once determined liable an employer will receive quarterly tax & wage reports each quarter.

**You are liable to pay NH Unemployment Tax if you meet any of the following conditions:**

- You have quarterly payroll of $1,500 or more in a calendar year.
- You have one or more employees for a day (or portion of a day) during any 20 weeks in a calendar year.
- You are an agricultural employer and pay wages of $20,000 or more for agricultural labor in a calendar quarter or have 10 or more employees in 20 different weeks during a calendar year.
- You are a domestic employer with a cash payroll of $1,000 or more in a calendar quarter.
- You are liable for federal unemployment tax.(FUTA)
- You purchase the business of another liable employer and continue the business.

**Employee vs. Independent Contractor**

The department utilizes the "ABC Test" RSA 282-A: 9, III (a)(b)(c) in order to determine if an individual is in employment. Services will be considered “in employment” and unemployment insurance coverage be required, unless and until the employer is able to demonstrate that all three parts of the so-called "ABC Test"are met.

Those tests are:

A. Such individual has been and will continue to be free from control or direction over the performance of such services, both under his contract of service and in fact; and

B. Such service is either outside the usual course of the business for which such service is performed or that such service is performed outside of all the places of business of the enterprise for which such service is performed; and

C. Such individual is customarily engaged in an independently established trade, occupation, profession or business.

All 3 parts of the test must be passed in order for an individual to not be in employment. It is possible to not be an employee for IRS purposes, but still have services be considered "in employment" under the " ABC Test". Merely signing a contract indicating the person is an independent contractor does not automatically make an individual an independent contractor.
If you conduct business in NH you may be subject to the two business taxes described below. Please note that NH does not have an income tax on an individual’s reported W-2 wages, however income earned as an independent contractor is subject to these taxes as well if all of your business revenue exceeds $50,000 from all sources within and outside the state combined.

Certain statutes define ‘Employee’ and ‘Independent Contractor’ for the Department of Revenue Administration.

Rev 301.13 “Employee” means any person performing services for a business organization for which compensation is provided except that it does not include a director of a corporation acting in such capacity or an independent contractor.

Rev 301.17 “Independent contractor” means a person who:
   (a) Exercises an independent employment;
   (b) Contracts to do work for multiple business organizations that are not related parties;
   (c) Holds himself or herself out to the public as an independent contractor in the regular course of business; and
   (d) Meets one of the following criteria:
       (1) Has been granted independent contractor status by the Internal Revenue Service for federal income tax purposes; or
       (2) Works according to his or her own judgment or methods, without being subject to any employer except as to the results of the work and, has the right to employ and direct the action of other workers independently of such employer and freed from any superior authority to say how the specified work will be done.

Business Profits Tax

What is it? An 8.5% tax, for taxable periods ending on or after July 1, 2001, is assessed on income from conducting business activity within the state. For multi-state businesses, income is apportioned, using a weighted sales factor of 2 and the payroll and property factors. Organizations operating a unitary business must use combined reporting in filing their NH return.

Who pays it? Any business organization, organized for gain or profit carrying on business activity within the state is subject to this tax. However, organizations with $50,000 or less of gross business income from all their activities are not required to file a return.

When is the return due? Corporate returns are due on the 15th day of the 3rd month following the end of the taxable period. Proprietorship, partnership and fiduciary returns are due on the 15th day of the 4th month following the end of the taxable period. Non-profit returns are due on the 15th day of the 5th month following the end of the taxable period.

Do I have to make estimated payments? Yes, if your estimated tax liability exceeds $200. Four estimate payments are required, paid at 25% each on the 15th day of the 4th, 6th, 9th and 12th month of the taxable period.
**What is it?** A 0.75% tax is assessed on the enterprise value tax base, which is the sum of all compensation paid or accrued, interest paid or accrued, and dividends paid by the business enterprise, after special adjustments and apportionment.

**Who pays it?** Enterprises with more than $150,000 of gross receipts from all their activities, or an enterprise value tax base more than $75,000, are required to file a return.

**When is the return due?** Corporate and combined returns are due on the 15th day of the 3rd month following the end of the taxable period. Proprietorship, partnership and fiduciary returns are due on the 15th day of the 4th month following the end of the taxable period. Non-profit returns are due on the 15th day of the 5th month following the end of the taxable period.

**Do I have to make estimated payments?** Yes, if your estimated tax liability exceeds $200. Four estimate payments are required, paid at 25% each on the 15th day of the 4th, 6th, 9th and 12th month of the taxable period.

**How does Employee Misclassification affect me?**

If for example you file as a corporation, federally the compensation you pay to an employee or an independent contractor is a deductible expense. The cost of having an employee is generally higher than using an independent contractor. However these costs are usually deductible expenses federally and thus they would reduce one’s BPT liability to a greater extent. A corporation may have higher profits subject to the BPT if they utilize independent contractors.

The compensation paid to an employee by the corporation is taxable to the corporation under the BET if the filing threshold is met. The corporation would pay the tax. However, if the compensation is paid to an independent contractor, he or she is responsible for filing the BPT and/or the BET if the applicable filing thresholds are met.
If you have an employee, even if it is only part-time or a family member, then you have certain legal duties to assure the safety and benefits of the worker. For example, you must get private insurance covering **workers’ compensation**, to assure that if the worker is hurt on the job, he or she gets prompt payment of the modest benefits required by law. Also, you must pay the government to cover possible future **unemployment compensation**.

Here is a checklist of items to consider, to be sure you comply with the law. Double check with your business advisors (legal, insurance and financial) if you need help. Or, contact the government offices listed here.

**New Hire Checklist**

- Workers Comp required when there is one or more employees (full or part-time)
- I-9’s or Documents verifying Employment Eligibility
- W-4 for IRS
- Register with NH Employment Security within 30 days of first providing employment
- New Hire Reporting (NH Employment Security)
- Written Notifications signed by the employee
  - Rate of pay-Hourly/Salary, Commissions, Piece rates, Flat rates
  - Payday
  - Fringe Benefits Policy
- Youth Employment
  - (12-15) Certificates
  - (16-17) Parental Permissions
  - Allowable hours of work
  - Hazardous Orders
- Payroll information
  - Written Authorization for legal deductions under RSA 275:48
- Payment Options
  - Paper Check
  - Direct Deposit
  - Paycard
- Waivers as applicable (lunch, day of rest, hours for nurses)