

Worker Misclassification Poses Large Perils For NJ Cos.

By **Brent Bouma and Peter Shapiro** (September 22, 2022)

Since early 2020, the New Jersey Legislature has passed several pieces of legislation aimed at furthering the Garden State's efforts to curb and remedy employee misclassification. This spotlight on worker misclassification has been a priority of Gov. Phil Murphy's administration since he was first elected.



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This appetite for protecting workers is exemplified by Murphy's Executive Order No. 25, issued on May 3, 2018, which established a misclassification task force.[1]

The task force subsequently issued a report that identified 12,315 workers who were misclassified, over \$400 million in wages that were underreported, and almost \$14 million in contributions to unemployment, disability, family leave insurance and workforce funds that were similarly underreported.[2] These findings produced quick action in Trenton.



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On July 8, 2021, Murphy signed a four-bill legislative package that furthered the state's efforts to police worker misclassification. The ramifications of these bills on companies that operate in New Jersey are profound.

A.B. 5890/S.B. 3920, for example, empowered the commissioner of the Department of Labor and Workforce Development to issue broad stop-work orders to employers determined to have violated the wage and hour laws across "all of the employer's worksites and places of business." [3]

Whereas prior orders could only extend to the specific place of business or employment where the violation existed, the state labor department can now wield broad power to issue stop-work orders across all of an employer's work sites in the state. In addition, the resulting stop-work orders may now remain in effect until the employer becomes compliant and pays any penalties due.

The labor department, now armed with these expansive new powers, has been prolific. In fact, in the three years since Murphy signed the legislation, the department has issued 71 stop-work orders, covering 16 of New Jersey's 21 counties, resulting in the payment of nearly \$1 million in back wages owed to 235 workers.[4]

Seemingly no industry is protected from this increased scrutiny, as the labor department proudly states that these 71 stop-work orders "have been used to shut down work sites of all types, such as construction jobs, restaurants, an internet radio station, and medical offices." [5]

Labor Commissioner Robert Asaro-Angelo recently expounded on the department's enhanced power with a warning to employers: "With the authority to issue stop-work orders as soon as we identify a violation, [we] gained the ability to shut down a job when it finds workers are being exploited." [6] As shown, this expanded power has yielded far-reaching results.

The New Jersey judiciary, for its part, has aided in this expansion.

Under the state's Unemployment Compensation Law, the so-called ABC test is used to determine whether certain workers are properly classified as employees or independent contractors.[7] Under the ABC test, services performed by an individual for remuneration shall be deemed employment unless the following factors are satisfied in full:

(A) Such individual has been and will continue to be free from control or direction over the performance of such service, 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.[8]

All three prongs must be met for a worker to be considered an independent contractor under the Unemployment Compensation Law.

While the ABC test is statutory, the New Jersey Supreme Court has adopted it to determine whether an individual is an employee or an independent contractor for the purposes of resolving wage payment and wage and hour claims.[9]

The court's Aug. 2 decision in *East Bay Drywall LLC v. Department of Labor and Workforce Development*,[10] is also significant because, after conducting the requisite fact-specific analysis, the court held that a contractor's establishment of a separate corporate structure through which to render services may not suffice to establish independent contractor status under the ABC test if the other prerequisites are not met.[11]

Thus, according to the *East Bay* decision, a putative independent contractor's creation of a limited liability company or corporation is not, standing alone, sufficient to show an independently established business under prong C of the ABC test.

East Bay also could not meet its burden in contesting the labor department's determination that some subcontractors were actually employees in light of the principle that the Unemployment Compensation Law is remedial and its provisions are construed liberally. The company's position was further undermined by its inability to show that the workers were able to maintain an independent business under prong C of the ABC test, including as to such factors as

the duration and strength of the business, the number of customers and their respective volume of business, or the number of employees; nor does it address the amount of remuneration each "drywall subcontractor" received from *East Bay* compared to that received from others for the same services.[12]

Thus, *East Bay* could not satisfy the ABC test notwithstanding the existence of separate entities through which the workers rendered services. This was also due to the court's concern that some businesses may require workers to assume the appearance of an independent business entity in name solely to support classification as an independent contractor.

In light of the Legislature and Murphy's focus on worker misclassification, as well as the judiciary's embrace of the statutory ABC test for various forms of worker classifications — as exemplified in the recent East Bay decision — New Jersey businesses that classify some workers as independent contractors should consider regular reevaluations to ensure compliance with the ABC test as applied under the Unemployment Compensation Law.

With the Department of Labor and Workforce Development and its auditors firing on all cylinders, businesses that fail to properly classify their workers may find themselves required to retroactively make employer contributions to unemployment compensation and temporary disability benefit funds if it is determined that they incorrectly classified their workers. These businesses may also run the risk of being issued stop-work orders encompassing all work locations, and exposure to civil fines.

Because worker classification ordinarily requires a fact-specific analysis, any business that relies on a singular prong of the ABC test independently, rather than satisfying all three factors, may be doing so at its peril.

And for companies, this peril is ever-increasing.

A.B. 5890/S.B. 3920, for example, permits the state labor department to assess civil penalties of \$5,000 per day against an employer for each day that it conducts business operations in violation of a stop-work order.[13] Since the department's authority to issue stop-work orders has been enhanced, employers faced with a stop-work order will be exposed to both economic penalties from the state and huge damage to their operations because they will be unable to conduct their work.

The law also hits the employer's bottom line because it requires companies to pay affected employees for the first 10 days of work lost because of the stop-work order, even though work is not being completed.[14] Notably, even a company's request for a hearing on the merits does not automatically stay the effect of the order or the penalties that follow.[15]

Also of note, these increased penalties and powers are not limited to stop-work orders, as even a company's failure to maintain wage records may trigger fines of at least \$1,000 per day until a company is in compliance.[16]

In 2022 alone, the state labor department has issued five press releases identifying 18 stop-work orders and related civil penalties issued to various companies performing work in the Garden State.[17] As a result of the spotlight on these issues and the department's aggressive enforcement, the importance of understanding and abiding by the ABC test, as well as ensuring the proper classification of workers for businesses that operate in New Jersey, cannot be understated.

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[1] Executive Order 25. May 3, 2018. Accessed 9/20/22. <https://nj.gov/infobank/eo/056murphy/pdf/EO-25.pdf>.

[2] Report of Gov. Murphy's Task Force on Employee Misclassification, July 2019, p. 7. Accessed 9/20/2022. <https://www.nj.gov/labor/assets/PDFs/Misclassification%20Report%202019.pdf>

[3] See N.J.S.A. 34:1A-1.17(c)(1).

[4] 17 August 2022. Trenton, New Jersey. "NJDOL Uses Expanded Powers to Stop Worker Exploitation at Job Sites." New Jersey Department of Labor & Workforce Development. Accessed 9/20/22. https://www.nj.gov/labor/lwdhome/press/2022/20220817_expandedpowers.shtml

[5] Ibid.

[6] Ibid.

[7] See N.J.S.A. 43:21-19(i)(6)(A)-(C).

[8] See N.J.S.A. 43:21-19(i)(6).

[9] Hargrove v. Sleepy's LLC, 220 N.J. 289 (2015).

[10] East Bay Drywall, LLC v. Department of Labor and Workforce Development, Docket No. A-7-21 (August 2, 2022).

[11] East Bay at * 23-25.

[12] East Bay at * 24.

[13] See N.J.S.A. 34:1A-1.17(c)(1).

[14] See N.J.S.A. 34:1A-1.17(c)(2).

[15] See N.J.S.A. 34:1A-1.17(c)(1).

[16] See N.J.S.A. 34:1A-1.17(b).

[17] New Jersey Department of Labor & Workforce Development. Press Releases. Accessed 9/21/22. <https://www.nj.gov/labor/lwdhome/press/>.