



Worker Classification Overview and Updated

**Senior Business Administrators Forum
December 15, 2021**

Agenda

- Independent Contractor Definition
- Biden Administration's Regulatory Overview
- High Level Summary of Issues
- Considerations on the State Level
- Worker Misclassification Cases
- PwC – Most Recent Exposures in Higher Ed
- Fines and Penalties – Federal Level
- Independent Contractor Expenditures
- Repercussions
- Recommendations and Next Steps

Independent Contractor Defined

True independent contractors are generally given a task that needs to be accomplished, a timeframe within which to complete it, and nothing else.

Biden Administration's Regulatory Overview

- The Biden campaign's top 10 issues included a focus on misclassification of workers
 - “Too many working Americans falling through the cracks”
 - Administration considers all individuals employees until proven otherwise
- Biden rescinds Trump ERA plan
 - Current focus on intentional misclassification and stricter enforcement of existing laws
- Bill making its way through Congress would institute the ABC Test at the Federal Level for certain labor rules
 - ABC Test, which is used in most state audits, is more rigorous than tests currently used at the Federal Level
- Biden's 2022 budget plan highlighted his administration's commitment to employment protection to workers who have been classified as 1099 independent contractors
- IRS Tax Exempt Org Division priority
 - Examinations to determine underreporting and underpaying FICA and federal income taxes and exclusion from employer retirement plans

ABC Test

- A worker must meet all three criteria to be considered an independent contractor:
 - A. The worker must be free from the employer's control or direction in performing the work.
 - B. The work must be outside the usual course of the employer's business.
 - C. The worker must be customarily engaged in an independently established trade, occupation, profession, or business.

High Level Summary of Issues

- Classification based on individual and not project
 - Scope of work and payment terms often exceed or are different from the original proposal
 - Independent contractors continue to be paid as such year after year without further review

<i>Vendors paid in 2019, 2020 and 2021</i>		
School/Center	# Vendors	% to Total
Wharton	80	18%
PSOM	63	15%
SAS	50	12%
Penn Praxis/ Penn Press	32	7%
Weitzman	29	7%
GSE	27	6%
All Other	152	35%
Total	433	100%

High Level Summary of Issues (Cont.)

Limited Engagement

- Limited engagement* or independent contractor payments made to employees and students
 - *Made up term at Penn; LEs are Independent Contractors
- Work being performed before documentation reviewed
 - Leads to Penn paying individuals who should not be classified as LE/independent contractors, or for whom there are other payment-related issues
 - Independent Contractors engaged outside the US require additional review by GSS as in-country requirements differ by country

<i>Limited Engagements Signed After Services Provided - Q1 CY2021</i>		
School/Center	#	% to Total
PSOM	55	12%
SAS	38	8%
GSE	36	8%
All Other	134	30%
Total signed after services provided	263	58%
Total LE Contracts Signed	454	

Considerations on the State Level

- Over half of the states use the ABC Test.
- Cross-agency and cross-state coordination has been useful in identifying employers who break labor laws.
 - In 2019, labor departments in Pennsylvania, New Jersey and Delaware agreed to share information and coordinate their enforcement efforts.

Worker Misclassification Cases

- Vox Media
 - \$4 million to settle three class-action lawsuits in 2021
 - Bloggers accused Vox of wrongfully classifying them as independent contractors and depriving them of minimum wage and overtime
- National Football League
 - First suit - Security representatives sued NFL for intentional misclassification for overtime wages, expense reimbursements, pension and welfare benefits, and damages.
 - Second suit – further pointed out that the NFL was unjustly enriched by avoiding its obligations of paying Social Security and Medicare taxes.
 - The courts granted arbitration in both cases – 1st suit was settled for an undisclosed amount in 2020; 2nd suit is still pending

PwC–Most Recent Exposures in Higher Ed

- **Former employees hired back** by university as independent contractors and **challenged by the IRS**
- **Adjunct Faculty members** being treated as independent contractors paid via 1099 and **challenged by the IRS**
- In both cases, the universities were required to reclassify them as employees
- In these and other exams, PwC's requested remediation is to reclassify prospectively for *most* of the worker's the IRS challenged
 - Avoided the imposition of penalties and interest
- Instances existed where the university disagreed with the IRS determination and had support for treating workers as nonemployees and the IRS agreed

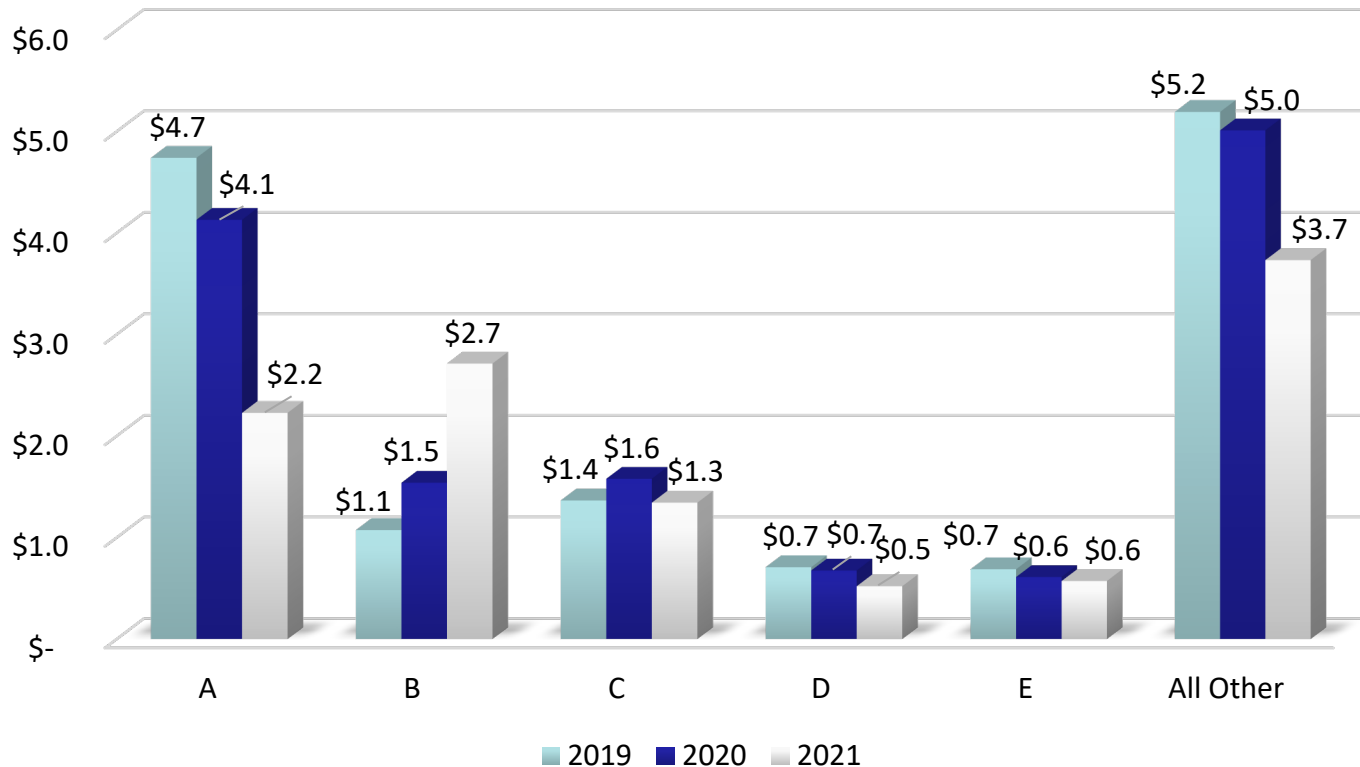
Fines and Penalties – Federal Level

- Fines are based upon whether the DOL and the IRS determine the misclassification was unintentional or intentional/fraudulent

Employer Fines and Penalties	
Unintentional Misclassification	Intentional or Fraudulent Misclassification
Reclassification of Wages	Reclassification of Wages
Penalties of 1.5% of wages	Penalties of 20% of wages
40% of the FICA Taxes (Social Security & Medicare) that were not withheld from the employee	100% of the FICA Taxes (Social Security & Medicare) that were not withheld from the employee
100% of the matching FICA that employer should have paid	100% of the matching FICA that employer should have paid
Interest is also accrued on these penalties daily from the day they should have been deposited.	Interest is also accrued on these penalties daily from the day they should have been deposited.
	\$1,000 per misclassified worker & one year in prison

Independent Contractor Expenditures

IC Expenditures by School/Center



Repercussions

- Fines and Penalties
 - Borne by respective departments, schools, and centers
- Damage to Penn's reputation
 - Negative media attention
- Reclassify all Independent Contractors to employees
- Potential annual review for 3 consecutive years of 1099s issued for non-employee compensation
 - Support documentation must be retained and provided by the departments, schools, and centers

Recommendations and Next Steps

- Engage with PwC to perform audit
 - Review our current policy and procedures
- Development of electronic flow of classification process
 - Creation of an electronic SPE & SPQ forms
 - Process improvements to the Penn Marketplace – simplified onboarding, payments, and preset deactivation dates for individual service providers
- Annual audit of process compliance
 - Development of dashboard and follow-up procedures
- Assign dedicated Employee responsible for:
 - Final review of ***all*** Worker Classification determinations & Independent Contractor agreements
 - Training of school and center HR administrators
 - Management of website
 - Communications to university community
- Pursue Outsourcing

Resources

- [Financial Policy #2319.4](#) Procurement and Reporting of Independent Contractors
- [Financial Policy #2319.3](#) Limited Engagement Policy
- [Procedural Guide](#) for Independent Contractors and Limited Engagements
- HR ISP Helpdesk: ISPClassification@upenn.edu
- [Global Support Services](#) (GSS) website
- [Service Provider Questionnaire](#) (SPQ)
- [Service Provider Evaluation Worksheet](#) (SPE)
- Limited Engagement Agreement – [US Persons](#)
- Limited Engagement Agreement – [Services within the US - NRAs](#)
- Limited Engagement Agreement – [Services outside the US](#)

Questions?

