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Why Employers Should Be Diligent with Employee Classifications

By James Hammerschmidt

This is a bit of a trick question. The short answer is no. If a worker is correctly classified as an independent contractor, the worker is not a "covered employee" under the Maryland Workers' Compensation Act and the employer is not liable for the worker's on-the-job injuries. However, as we often blog, the classification of independent contractors is tricky business and if the employer gets it wrong and misclassifies the worker, it may be responsible for the worker's injuries under at least two different scenarios according to a recent decision by the Maryland Court of Appeals in *Elms v. Renewal by Anderson*.

Briefly, the facts: Elms was a licensed home improvement contractor with his own unincorporated home improvement business, Elms Construction. Elm's carried workers' compensation insurance but did not include himself on the policy. He derived approximately 80-85% of his income from window installations for Renewal. As a contractor for Renewal, Elms was subject to several requirements, including wearing shirts bearing Renewal's logo, placing Renewal signs in customers' yards, and obtaining all supplies and materials from Renewal's warehouse. Elms did use his own trucks and usually his own tools. Elms and his workers also underwent training from Renewal and his jobs were spot checked by Renewal who could, and did, require Elms to make corrections. Renewal expected Elms to adhere to the policies and instructions contained in the "Installation Job Expectations" manual, and it required customers to rates Elms' performance on report cards at the end of each installation. Further, Renewal provided Elms with a schedule of jobs that included the address of the sites, the names of the residents, and the time frame for each job.

As Renewal's luck would have it, Elms was injured installing a window at a Renewal customer's home when he fell off a ladder and filed a workers' compensation claim alleging that he was a common law employee of Renewal. Renewal claimed it wasn't liable because Elms was an independent contractor. The Court disagreed.

The Court first found that Elms was a common law employee entitled to workers' compensation benefits under Renewal's policy. The Court came to this conclusion quickly, noting that Maryland law presumes an individual is a covered employee, and that application of the common five (5) factor test – power to select and hire, payment of wages, power to discharge, power to control employee's conduct, and whether work is part of the regular business of the employer – supported a finding that Elms was an employee of Renewal. The Court reiterated that the power to control employee conduct is the most important factor and noted that Renewal's control over Elms was clear. The Court specifically noted that Renewal controlled the dates and times of all Elms' schedule of jobs, provided detailed training and instructions (down to the type of screws, shims, caulking, and molding), spot checked Elms' work, required Elms to wear Renewal logos, and expected Elms to adhere to Renewal's written policies and instructions.

The Court then noted that § 9-508 of the Maryland Workers' Compensation Act, commonly referred to as the "statutory employer provision," creates an employer/employee relationship by statute, which is separate and apart from, and in addition to, the common law employer/employee relationship. This section applies when the following conditions are met: (1) a principal contractor; (2) who has contracted to perform work; (3) which is part of its trade, business or occupation; (4) contracts with any other party as a subcontractor to do all or any part of the work. When all of the conditions are met, under the Act, an employee of a subcontractor will be able to recover workers' compensation benefits from a principal contractor at the "statutory employer." As the Court explained, "'the purpose of the statutory employer provision is the protection of the injured worker who might otherwise receive no compensation for work-related injuries if the worker's immediate employer had not obtained workers' compensation coverage and had little resources to pay damages in a personal injury action.'" Accordingly, by its terms, § 9-508 only operates to make a principal contactor liable when an employee is unable (apparently for whatever reason) to recover from his direct employer, the subcontractor.

The *Elms* Court summed up its analysis stating, "[i]n our view, the statute does not 'abrogate' the common law employment relationship; instead, it creates a potential alternative relationship where the common law employer/employee relationship does not exist between the injured worker and the principal contractor."

Lesson for Employers: *Errors in misclassification of workers can lead to a long list of unforeseen problems that can be very costly, including liability for unpaid taxes and unemployment insurance contributions; liability for unpaid wages, overtime & benefits, liability under Maryland's Workplace Fraud Act; ERISA claims; liability under most employment statutes, such as Title VII, ADAAA, FMLA, ADEA and NLRA; and liability for workers' compensation benefits. Decisions about whether to treat a worker as an independent contractor versus an employee must be analyzed carefully and should not be made based on a perceived cost savings, which may well end up being short-sighted and more costly.*

