



EMPLOYMENT AND  
ECONOMIC DEVELOPMENT

# Unemployment Insurance and Worker Misclassification

Attorney General's Advisory Task Force on Worker Misclassification  
October 25, 2023



# Agenda

- A brief intro to Unemployment Insurance
- Federal law and program responsibilities
- Minnesota law and program responsibilities
- Audits

# Basic unemployment insurance policy

“...The public good is promoted by providing workers who are unemployed through no fault of their own a temporary partial wage replacement to assist the unemployed worker to become reemployed...” (MN Statutes 268.03)

- Eligibility based: primarily laid off – but also quits and discharges where the worker did not cause their own unemployment
- Temporary: up to 26 weeks
- Partial wage replacement: about ½ of weekly wage up to statutory maximum (currently \$857)
- To become reemployed: able to work, available for work, looking for work or something substantially similar (training for work)

# Funding – taxes and reimbursements

- Benefits are funded by a payroll tax paid by MN employers into a trust fund
- Most employers pay based on program use (Experience Rated or “Taxpaying”):
  - Taxable wage base – indexed, \$40,000 (2023)
  - Base tax – variable based on fund health, currently 0.1%
  - Experience rating – variable 0.00% to 8.9%
  - Additional Assessment – variable, based on fund health, currently 0.0%
  - Special Assessment – variable, based on fund health, currently 0.0%
- A few employers reimburse the program for actual expenses (“Reimbursing”)
  - State, political subdivisions, Tribal Governments and some nonprofits

# UI is a Federal-State Partnership

- Created by the Social Security Act of 1935
- Paid for by the Federal Government, administered by the states
- State's UI law must conform with federal standards as set by, primarily, the US Department of Labor (USDOL) and IRS
- States must administer UI programs in a manner that complies with federal law, directives, and performance standards established by USDOL
- States may only use their federal funding for program activities that are expressly authorized by USDOL via the Resource Justification Model (RJM), the funding mechanism used for UI
- RJM prohibits states from expanding activities beyond levels set by USDOL (and penalizes inefficiency)

# Federal law and UI program responsibilities

- Misclassification of workers falls primarily under UI Tax administration (viewed in context of a tax avoidance scheme)
- No direct federal requirement for states regarding misclassified workers. USDOL Tax Performance System (TPS) sets the standards for how audits are conducted
- Part of the standard includes detecting and correcting un-reported, under-reported and mis-reported wages
- TPS defines what “counts” as an audit, and therefore what work USDOL will pay states to perform
  - Must be basis to believe that an employer/employee relationship existed for a “countable” audit
  - State UI programs could not, for instance, expand their audit activities to include all possible improperly classified work in the state

- Definitions of employment, covered employment, covered agricultural employment, non-covered employment, and wages are found in [268.035](#)
- Non-covered employment includes:
  - Self-employed individuals
  - Churches
  - Corporate officers
  - Agricultural and domestic employment has thresholds
  - Several other categories
- Most employment in the state is “covered” by UI law
- Any entity that has covered employment is required to report wages quarterly and pay quarterly UI tax based on those wages

# Covered employment and independent contractors

- Independent contractors and self-employed individuals are not covered by UI
  - We don't get wage detail submissions for them
  - Small business owners (sole proprietorships, partnerships, LLCs) and farmers are considered self-employed
  - Gig work is not a formal classification - could be self-employment, could be informal/casual employment
- “Misclassified” is not defined in statute, but generally would be a worker who was being treated as a self-employed individual or independent contractor, but was found by UI to have been an employee
  - Five-factor test for employee / independent contractor in UI Rules ([MN Rules 3315.0555](#))
- No specific requirement under state UI law that misclassified workers be detected and corrected on tax side
  - This is handled by program direction and the funding mechanisms set by USDOL
- If an individual applies for benefits and notes that wages are missing from UI records, UI has an affirmative obligation to follow up to find wages
  - In most cases, wages are just listed under the wrong name or SSN, but where an employer did not report employment, and audit is performed, UI issues a formal, appealable determination regarding coverage of the employment
  - All tips regarding misclassified workers are investigated just like any information received from another agency



- Basics
  - UI auditors perform around 1,800 audits per year when fully staffed
  - Until the pandemic, all audits had to be performed in person, which was a barrier - now they can be done virtually
- Two types of audits
  - Random – to measure general compliance of employer population in line with federal requirements
  - Selected – based on identification of missing wages when applications for benefits are filed, tips, or data analysis
- Random audits
  - Generally, random audits find that most employers comply, but mistakes are detected
  - Most errors are misunderstanding of employment definitions (these differ a bit by program, state, and federal law)
  - Where misclassification occurs, it's common for both parties to have chosen the nature of the relationship
  - Over the last decade or so, random audits were more likely to result in a small refund than additional taxes
- Selected audits are more likely to find misclassification (not surprisingly)

# Some Observations from Audits

- Remember, we're auditing employers who have submitted some level of wage detail
- UI's only real source of potentially misclassified work is benefit applications, which are a very small proportion of the workforce
- UI can find errors and mistakes along with misclassifications for those employers that are otherwise compliant – mostly, we find opportunities to educate
- Most tips come from disgruntled acquaintances and business competitors
- Some workers UI finds to be misclassified prefer to be treated as independent contractors