



# *COMMONWEALTH of VIRGINIA*

## *Department of Taxation*

December 30, 2021

The Honorable Ralph S. Northam  
Governor of Virginia  
Patrick Henry Building, 3<sup>rd</sup> Floor  
1111 East Broad Street  
Richmond, Virginia 23219

Members of the Virginia General Assembly  
Pocahontas Building  
Richmond, Virginia 23219

Dear Governor Northam and Members of the Virginia General Assembly:

In 2020, the General Assembly enacted House Bill 1407 (2020 Acts of Assembly, Chapter 681) and Senate Bill 744 (2020 Acts of Assembly, Chapter 682) which established the Virginia standard for classifying workers performing services for remuneration as employees or independent contractors. The provisions of this legislation had an effective date of January 1, 2021. The legislation also requires the Department of Taxation (Virginia Tax) to publish an annual report regarding its activities regarding the misclassification of workers. The report is due on or before the end of the calendar year.

### **Overview of the Misclassification of Workers Program**

As required by the 2020 legislation, an individual who performs services for an employer for remuneration is an employee for tax purposes unless demonstrated to be an independent contractor. In addition, statute requires that Virginia Tax use the IRS guidelines in determining whether a worker is an employee or independent contractor.

### **Civil Penalties Established for Misclassifying Employees**

If Virginia Tax determines the employer inappropriately classifies an individual as a contractor vice employee, the employer will be subject to the following monetary penalties:

- \$1,000 per misclassified individual for instances of misclassification from the first audit of an employer;
- \$2,500 per misclassified individual for instances of misclassification from the second audit of an employer; and
- \$5,000 per misclassified individual for instances of misclassification from the third audit of an employer and on any subsequent audits of such employer.

The monetary penalties apply to findings of worker misclassification that occur on or after January 1, 2021.

### **Debarment Provision for Misclassifying Employees**

When Virginia Tax determines that an employer failed to properly classify an individual as an employee, we are required to notify all public bodies and covered institutions for information purposes of the name of the employer. If we find instances of misclassification on subsequent audits, we are also required to notify all public bodies and covered institutions. Following this notification, they are prohibited from awarding a contract to this employer and to any firm, corporation, or partnership in which the employer has an interest for:

- A period of up to one year from the date of the notice for violations found during a second audit, and
- A period of up to three years from the date of the notice for violations found during a third audit or any subsequent audits.

For purposes of the debarment provisions, “covered institution” means a public institution of higher education.

### **Calendar Year 2021 Program Activity**

The COVID-19 pandemic negatively affected the planned timeline for hiring and training staff. However, once the staff were onboard and trained, they analyzed data for 155 potential candidates for worker misclassification audits resulting in 46 audits now in progress. In addition, Virginia Tax has sent over 100 initial inquiry letters to employers asking for information regarding employee classification. As of this date, the agency has collected \$74,557 in tax, interest, and penalties. This includes \$14,000 representing the statutory penalty for the misclassification of 14 employees.

In addition, Virginia Tax continues to work with other state agencies regarding best practices to exchange data relevant to misclassification. We have held several meetings with affected

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agencies to discuss educating taxpayers on worker misclassification and sharing of potential audit candidates. In addition, the Department of General Services provided a database of approximately 8,400 vendors to help us develop better predictive models for audit selection.

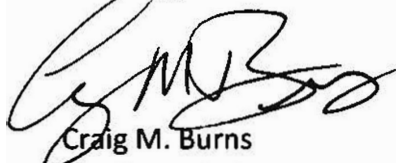
Finally, our taxpayer outreach strategy for this program has focused on driving education and awareness among business owners and tax professionals so that we can prevent misclassification before it occurs. To date, our outreach materials have included web content, a fact sheet, social media posts, a standalone PowerPoint deck, and articles in Virginia Chamber of Commerce publications.

The content starts with the basics – defining terms, explaining the changes to Virginia law, and setting expectations for what happens if a business is selected for a an audit. We have sought feedback from other agency participants in the working group to ensure our materials are meeting the audience’s needs. In addition, we continue to share a dedicated email address, [misclassificationofworkers@tax.virginia.gov](mailto:misclassificationofworkers@tax.virginia.gov), for any worker misclassification inquiries.

## Conclusion

Despite the challenges of starting a new program in a pandemic environment, Virginia Tax has implemented and administered a worker misclassification audit program that complies with House Bill 1407 and Senate Bill 744. We appreciate the assistance of all state agencies involved in the effort.

Sincerely,



Craig M. Burns  
Tax Commissioner

Cc: The Honorable K. Joseph Flores, Secretary of Finance  
Ms. Arleen Green, Assistant Commissioner for Compliance