

New Guidelines and Penalties for Classification of Employees and Independent Contractors

Effective January 1, 2008, the Illinois Employee Classification Act provides new guidelines for determining the proper identification of workers as employees or independent contractors. This Act also imposes more stringent penalties for the improper identification of employees as independent contractors.

Guidelines

Under this new Act, an individual performing services for a contractor is automatically considered an employee of the employer with two exceptions: (1) those individuals who legitimately satisfy the Act's test to qualify as an independent contractor; and (2) legitimate sole proprietors or partnerships. This Act applies to all contractors who are engaged in "construction", which is broadly defined to include any constructing, altering, repairing, remodeling or renovating of any land or structure.

In order to satisfy the first exception as an "independent contractor", the individual must: (1) be free from control or direction over the performance of services; (2) perform services outside the usual course of services performed by the contractor;

and (3) be engaged in an independently established trade or business. The Act provides a second exception for "legitimate" sole proprietors or partnerships performing services for a contractor.

Penalties

In addition to the right of the Illinois Department of Labor to enforce this Act, private parties are now authorized under the Act to file a lawsuit in circuit court without having to file a charge with the Illinois Department of Labor. In such a lawsuit, the "interested party" who has been damaged by the misclassification of employees now has the opportunity to seek back wages, back benefits, compensatory damages, liquidated damages, compensation for unlawful retaliation, punitive damages and attorneys' fees.

Other parties who can demonstrate damages arising out of an employee misclassification may also bring a private lawsuit under this Act. Such parties could include labor unions or another construction contractor who can claim that it was under bid by a violating contractor.

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FIRM HIGHLIGHTS

Paul M. Fullerton was installed as an Associate Judge of the 18th Judicial Circuit Court, DuPage County, Illinois on October 11, 2007. In accordance with the ethical rules governing attorneys and judges, Paul is no longer affiliated with CC&M as of the date of his installation.

Ross I. Molho will be speaking to new lawyers in connection with the DuPage Bar Association's "Basic Skills" program on December 7, 2007. The title of Ross' presentation is "The Ten Things You Wanted to Know About Employment Law."

CC&M represented a family owned business franchisee in the negotiation and sale of its business. The asset purchase transaction involved attorney **Deven Kane** and corporate paralegal **Jean Erhardt**.

Kenneth W. Clingen co-presented a National Business Institute Seminar to attorneys and accountants on Choice of Business Entity on September 26, 2007 in Oak Brook, IL. Ken's talk focused on the advanced tax aspects of choice of entity among "C" corporations, "S" corporations and limited liability companies.

Estate Planning for Everyone

Estate planning can mean counseling wealthy clients regarding avoiding estate taxes. But it actually includes far more and applies to virtually everyone, regardless of means. All clients want to control who will make decisions for them in the event of disability, provide for their loved ones and specify who will manage and receive their property at death.

Every adult, from age eighteen on, should sign Illinois Powers of Attorney for Property and Health Care. If an individual becomes disabled or unconscious because of illness or accident, someone needs to pay bills, sign tax returns and insurance documents, and make decisions related to health care and treatment. HIPAA makes it more difficult even for a spouse or parent of an adult child to obtain information and enforce decisions for someone else.

Do you REALLY understand who will receive your assets after your death? Clients assume that their spouse will receive everything. This may be true of joint assets, but NOT of assets in the client's sole name. The Illinois intestacy law (which provides a state-written will if you don't have one)

divides assets in your name among your spouse and children. Also, you need to provide for your children if your spouse dies with or before you. Finally, what if a child predeceases you leaving children? Most beneficiary designation forms for life insurance and retirement assets would leave everything to your surviving children, to the exclusion of the

grandchildren whose parent is gone.

Are your children ready to handle an outright inheritance? A will or trust agreement provides that assets remain in trust for the children while they are minors and well beyond

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majority until they are old enough to responsibly handle assets. Is one of your children involved in a bad marriage, has drug or alcohol issues, is financially disabled, or has creditor concerns? A will or trust can protect a child's inheritance by holding the assets in a discretionary trust, or creating a special needs trust for a disabled descendant to avoid losing state or federal aid.

The challenges and dynamics of today's families show the need for customized estate planning, regardless of the value of those families' estates.

by *Mary E. Callow & Delrose A. Koch*

Prepayment Penalties Upheld

Many commercial loan transactions, particularly mortgage loan transactions, include a prepayment penalty or “yield maintenance premium.” The prepayment penalty requires the borrower to pay the lender an amount based upon a formula or percentage of the loan balance if the borrower pays the loan prior to maturity.

In *River East L.L.C. v. Plaza L.L.C. et al.*, the U.S. Court of Appeals for the Seventh Circuit recently upheld a prepayment penalty. In so doing, the court reversed the District Court and sent a strong message about the ability of lenders to enforce provisions in commercial contracts that are clear and unambiguous. *River East* involved a commercial mortgage loan transaction. The loan provided that the borrower could prepay the loan if it paid a prepayment penalty based upon the greater of a percentage of the loan balance or a formula amount. Three years after the loan closing the borrower wanted to sell the property and repay the loan. The lender provided a payoff letter which included a prepayment fee equivalent to 38% of the original principal balance of the loan. The borrower paid the fee after the lender insisted, but began litigation against the lender.

The District Court determined that the prepayment penalty was an unreasonable liquidated damages clause because it did not bear any

relationship to the damages suffered by the lender from the prepayment. In reversing, the Court of Appeals adopted a different approach. It first noted that the Illinois Supreme Court had not addressed the issue of enforcement penalties in commercial mortgages. The Court of Appeals determined that the appropriate inquiry was whether the prepayment penalty was bargained for alternative performance by the parties. Ultimately the Court of Appeals determined that the prepayment penalty was enforceable.

This case is a stark reminder that borrowers should pay particular attention to prepayment penalty or yield maintenance clauses and test the fee calculation under a variety of prepayment scenarios. While it is unlikely that a lender will remove the clause entirely, the borrower may negotiate its terms. The borrower should verify that any prepayment clause is appropriately discounted for present value, contains the proper term for calculating the prepayment premium and uses an appropriate benchmark for calculating the spread between the interest rate on the loan and the benchmark rate.

If you have questions about loan-related prepayment penalties or yield maintenance premium, please contact CC&M.

by Kenneth W. Clingen

FIRM HIGHLIGHTS

Kenneth J. Vanko and **Steven A. Marderosian**

obtained a very favorable settlement of a bank’s suit to enforce a restrictive covenant against a CC&M client. The settlement eviscerated the scope of the restrictive covenant and saved the client many thousands of dollars in legal fees.

Ross I. Molho is scheduled to speak in Rockford, Illinois on January 8, 2008 at a professionally sponsored seminar by Lorman Education Services entitled “Employee Discharge and Documentation in Illinois.” One week later Ross will be speaking in Itasca, Illinois on January 15, 2008 in connection with a seminar entitled “Prevailing Wage Law in Illinois.”

CLASSIFICATION

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In light of these more stringent penalties for the improper identification of employees as independent contractors, businesses must ensure that they are following proper classification procedures for independent contractors.

by Timothy M. McLean

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Clingen Callow & McLean, LLC

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Timothy M. McLean, a partner at CC&M, concentrates his practice in business

counseling, commercial litigation and landlord-tenant law.

WHAT'S INSIDE? *Articles & Contributors*

Estate Planning for Everyone



Mary E. Callow, a partner at CC&M, practices in the areas of estate planning, estate administration, and succession planning for business owners.



Delrose A. Koch, of counsel at CC&M, concentrates her practice in the areas of tax and estate planning.



River East: Prepayment Penalties Upheld

Kenneth W. Clingen, a partner in the firm, practices in the area of corporate law, mergers and acquisitions and estate and succession planning for business owners.