

The Developing Employment Law of Independent Contractors



Presented By:



MAYNARDNEXSEN

Matt Stiles

March 5, 2024

AGENDA

- **What Is An ‘Independent Contractor’?**
- **The Law of Independent Contractors and DOL’s New Rule**
- **Assessing Potential Liability**
- **Best Practices for Businesses Utilizing Independent Contractors**
- **Action Items**

WHAT IS AN INDEPENDENT CONTRACTOR?

- **A Vendor of Services to Your Business**
 - **Most frequently another corporation:**
 - IT consultant
 - Internet Service Provider
 - After hours cleaning service
 - Maintenance
 - Skilled trades: plumbers, electricians, carpenters
 - **Provides a service beyond the capabilities or job descriptions of your employees**
 - **Receives a 1099**
 - ***Sometimes* this vendor is an individual:**
 - This is where legal risk arises

WHAT IS AN INDEPENDENT CONTRACTOR?

- **Independent Contractors Save You Money**
 - **Independent Contractors pay their own way:**
 - Employee recruitment, retention
 - Employee salaries, wages, overtime
 - Insurance and employee benefits
 - Cost of tools, special skills training, know-how
 - Taxes, fees, licenses, bonding
 - **They bear the risk of loss:**
 - If they make a mistake, the liability is theirs
 - If they expend more time than estimated, they lose the opportunity cost

WHAT IS AN INDEPENDENT CONTRACTOR?

What Do Individual Independent Contractors Have In Common with Business Independent Contractors?



**NOT
ENOUGH**

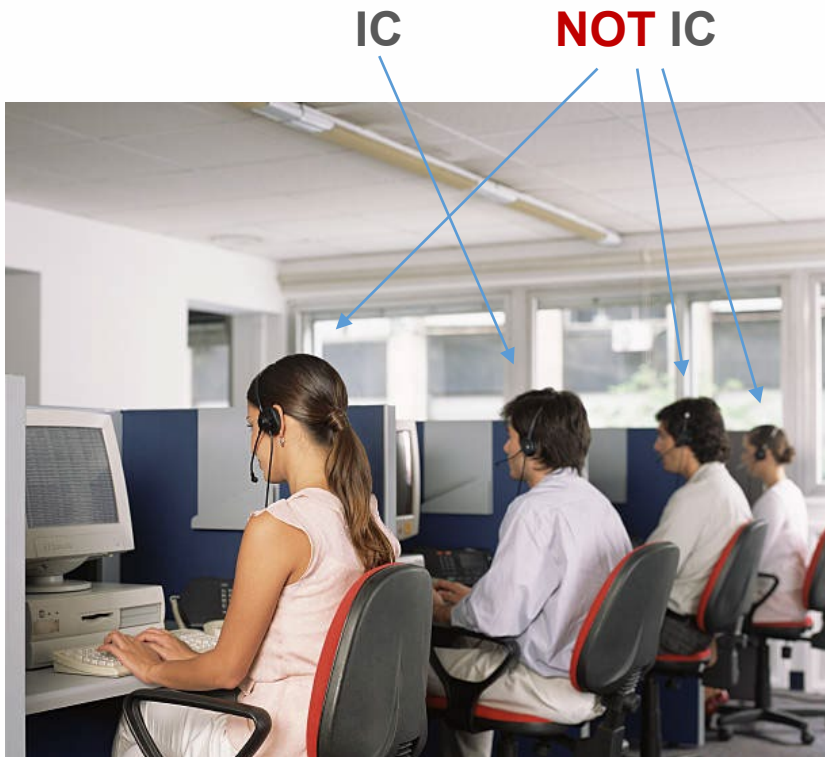
WHAT IS AN INDEPENDENT CONTRACTOR?



Consider the Plumbing Company Vendor

- Schedule & Availability
- Staffing: bring a helper?
- Skills, training, know-how
- Truck, tools, supplies
- Insurance, licensed, bonded
- Service contract/purchase order
- Pays its own employees wages, salaries, benefits, taxes
- Invoices fees and costs

WHAT IS AN INDEPENDENT CONTRACTOR?



Consider the Problematic Individual Independent Contractor

- Works at a location during hours specified by you
- Is solely responsible for the work assigned
- Performs work similar to regular employees
- Uses your computer, hardware, office furniture, tools, supplies, etc.
- Any mistakes are on you, not the Independent Contractor
- Paid a regular fee that looks like wages/salary
- Only works for you

THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

➤ US Department of Labor

- Wage and Hour Division; OFCCP; OSHA

➤ Internal Revenue Service

- Anyone receiving a W-2 and a 1099 from the same entity in the same tax year: second level IRS review

➤ National Labor Relations Board

- February 2022, US NLRB and DOJ filed an amicus brief in federal court arguing for a change in the law such that “gig economy” workers would have a right to “organize consistent with protections provided to workers by federal law.”

➤ EEOC

- All workers to be protected from discrimination, harassment, and retaliation



THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

- **State Labor Departments**
 - Unemployment
 - Workers Comp
 - State Disability Funds
- **State Revenue Agencies**
 - Withholdings
 - SUTA/FUTA
 - State disability or paid leave funds

THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

➤ Benefits Implications of Independent Contractors

- Employee benefit plans are typically only for “employees”
- A carrier might allow you to offer insurance to an independent contractor, but that doesn't mean you should do it
 - What eligibility definition in your Section 125 plan or other plan documents covers an independent contractor
 - If the independent contractor is truly in business for themselves, adding them to your plan could create an unintended multi-employer welfare arrangement (MEWA) regulated by both the states and federal government



THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

➤ Cross-Agency Cooperation

- DOL launched a “Misclassification Initiative” to attack this problem through “enforcement, education, and outreach”
- DOL Entered Memorandum of Understanding (MOU) with IRS
- Entered MOUs with 23 states to coordinate investigations, make referrals, share data:

Alabama, Arkansas, California, Colorado, Connecticut, Florida, Hawaii, Iowa, Kentucky, Louisiana, Massachusetts, Minnesota, North Carolina, Nebraska, New Hampshire, New Jersey, New Mexico, Oregon, Pennsylvania, Tennessee, Texas, Utah, West Virginia



THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

- **New DOL Rule Effective March 11, 2024, returns to pre-2021 framework that ask, whether as a matter of the “economic realities” a worker is economically dependent on the employer or is truly in business for themselves:**
- Opportunity for profit or loss based on managerial skill.
 - Investments by the worker and the potential employer.
 - Degree of permanence of the relationship.
 - Nature and degree of control.
 - Extent to which the work performed is an integral part of the potential employer’s business.
 - Skill and initiative.

No one factor is determinative and DOL and the courts should consider the “totality of circumstances.”



THE LAW OF INDEPENDENT CONTRACTORS AND DOL'S NEW RULE

➤ IRS 20-Factor Test for Lawful Independent Contractor Status:

- Level of Instruction
- Amount of Training
- Degree of Business Integration
- Extent of Personal Services
- Control of Assistants
- Continuity of Relationship
- Flexibility of Schedule
- Demands for Full Time Work
- Need for On-site Service
- Sequence of Work
- Requirements for Reports
- Method of Payment
- Payment of Business or Travel Expenses
- Provision of Tools and Materials
- Investment in Facilities
- Realization of Profit or Loss
- Work for Multiple Companies
- Availability to Public
- Control Over Discharge
- Right of Termination



ASSESSING POTENTIAL LIABILITY

➤ Getting Caught:

- Independent contractor **files for unemployment** upon conclusion of project
- Independent contractor has an **on-the-job injury**
- Independent contractor believes FLSA misclassification caused loss of wages, overtime and **makes an agency complaint or files a lawsuit**

➤ Potential liability:

- **A single unemployment claim** by a misclassified independent contractor can prompt a **company-wide audit for misclassification**, leading to a back-tax assessment for unpaid state unemployment taxes
 - Due to **cross-agency cooperation**, this can lead to a state revenue department audit, a federal DOL (FLSA) audit, and an IRS audit for back wages and back tax
- **On the job injuries can lead to penalties and fines** associated with not carrying workers' comp on the independent contractor in addition to OSHA penalties/fines
- Misclassification that leads to an FLSA (or comparable state law) wage claim can result in an **exponential expense associated with litigation** (where you pay the plaintiffs' attorneys' fees)



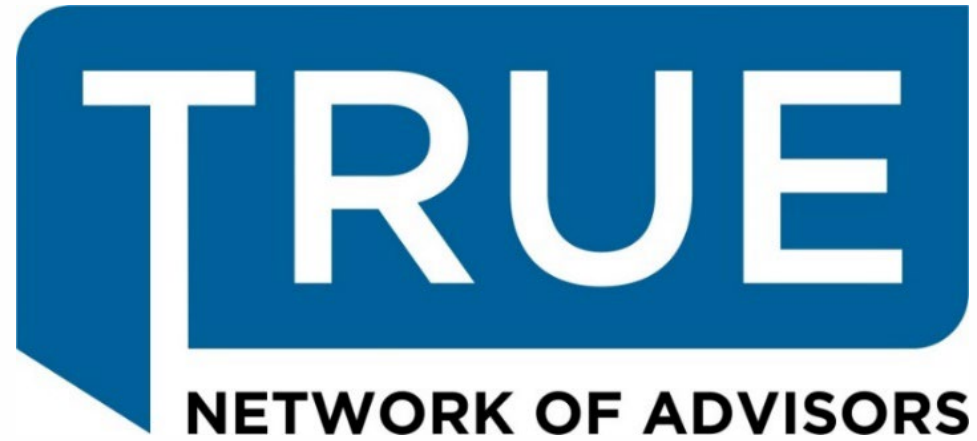
BEST PRACTICES

- Have a **gatekeeper** for any current, new independent contractors
- Have a **good written contract that tracks the principles of compliance**
- **Start by complying with both the New DOL Economic Realities Test and the Traditional 20-Factor IRS Test**
- **Other factors for limiting risk:**
 - Require that any independent contractor have a **corporation or LLC**
 - Require independent contractors to have a **business license**
 - Avoid using **non-compete agreements** in independent contractor agreements (confidentiality, some non-solicitations okay)
 - Do not employ someone in the **same tax year** you engage them as an independent contractor
 - Do not offer **employee benefits** to independent contractors



Action Items

1. Ask your accounting department to pull a list of all 1099s issued to an individual where SSN rather than EIN is shown on the 1099 – this is your audit list
2. Look at the written contract for these individuals to determine whether the relationship conforms—in writing—to the requirements under both the Economic Realities test and IRS 20-Factor test
3. Determine whether the actual relationship is consistent with the written contract
4. For any relationship that falls short:
 - Consider making an employee
 - Revise contract to conform to the rules
 - Encourage contractor to form an LLC or corporation going forward
 - Verify that contractor advertises and performs like services for other businesses



Matt Stiles

mstiles@maynardnexsen.com



MAYNARDNEXSEN