

USDOL's Final Rule on Independent Contractors

SMITH

So true . . .

"Few problems in the law have given greater variety of application and conflict in results than the cases arising in the borderland between what is clearly an employer-employee relationship and what is clearly one of independent entrepreneurial dealing."

N.L.R.B. v. Hearst Publications, 322 U.S. 111 (1944)

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Who cares?

- Workers (minimum wage, OT, unemployment, benefits)
- Employers (same as above, flexibility in staffing, reduces recruiting/retention costs)

- Federal and state governments
 - IRS/departments of revenue
 - Departments of labor
 - EEOC/NLRB
 - USCIS
 - Workers' comp/unemployment regulators



Who cares?



- Labor unions
 - ICs excluded from NLRA coverage and cannot organize

- Misclassified workers are potential dues-paying members
- The lawyers (especially plaintiffs' bar)
 - Misclassification cases are ripe for class actions
 - Big money potential

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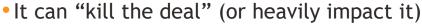
Why YOU should care . . .



- All it takes to spark a full-blown, multi-agency investigation:
 - One unemployment claim by contractor
 - One random, drive-by OSHA inspection
 - One complaint to state/federal DOL
- Liabilities can be significant







- Always a top due diligence issue in transactions
- Can affect marketability/value of the company
- Can lead to special indemnities/escrows that may not otherwise be necessary

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What's the worst that can happen?

- Liability for:
 - Penalties for failure to withhold income taxes and to pay FICA, FUTA, SUTA; interest; penalties; possible individual liability for execs
 - Employee benefits (unless plan has "Microsoft clause" and properly excludes misclassified workers)
 - Back wages for 2-3 years for MW and OT (longer in some states); liquidated damages; attorneys' fees





- Liability for:
 - Violations of federal employment laws (Title VII, ADA, FMLA, NLRA, etc.)
 - Immigration/I-9 issues (civil/criminal penalties)
 - OSHA violations (injunctive relief, civil/criminal penalties)
 - Workers' comp liability and penalties
 - Potential criminal penalties in some states

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How can we tell?

- Tests, tests, and more tests . . .
- IRS has a test ("old" 20 factor test; "new" three-prong test behavioral control, financial control, type of relationship)
- Federal and state courts have developed tests
- Federal and state agencies have tests for the laws they enforce





- Trump DOL's 2021 rule
 - 5 factors with focus on two "core" factors:

- Control (minimalized relevance of reserved/unexercised control)
- opportunity for profit/loss
- If those pointed to IC status, very likely IC without consideration of the other factors:
 - amount of skill required
 - degree and permanence of relationship
 - whether work part of integrated unit of production

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Recent evolution of USDOL test

- Biden DOL's new rule
 - Effective March 11, 2024
 - Return to "economic reality" test



Factor 1: Opportunity for profit/loss depending on managerial skill

• Can worker determine or negotiate pay for work?

- Does worker accept/decline jobs or choose order/time in which performed?
- Does worker engage in marketing, advertising, other effort to expand/secure work?
- Does worker make decisions to hire others, purchase materials/equipment, or rent space?

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Factor 1: Opportunity for profit/loss depending on managerial skill (cont.)

 Note that decision to work more hours or take more jobs when paid a fixed rate per hour or job does not reflect type of managerial skill contemplated by rule





- Are the worker's investments entrepreneurial in nature?
- No:
 - Costs of tools/equipment to do specific job
 - Costs of worker's labor
 - Costs that company imposes on worker
- Yes:
 - Expenditures that increase ability to do different or more types of work, reduce costs, expand market reach

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Factor 2: Investments by the worker and the employer (cont.)

- Worker's investments need not be equal to company's investments
- Focus should be on comparison to determine whether the worker is making similar types of investments (even on smaller scale) to suggest that worker is operating independently





- Suggestive of employee status:
 - Indefinite
 - Continuous
 - Exclusive of work for others
- Suggestive of contractor status:
 - Definite
 - Non-exclusive
 - Project-based
 - Sporadic

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Factor 4: Nature and degree of control

 Must consider exercised and reserved control over performance of work and economics of relationship

- Relevant factors include whether company:
 - Sets schedule, supervises performance of work, limits worker's ability to work for others
 - Uses technological means to supervise performance of work (via devices or electronically)
 - Reserves right to supervise or discipline worker, or places demands/restrictions that do not allow worker to work for others or to work when they choose
 - Exercises control over prices, rates for services, marketing of services provided by worker





- Actions taken for sole purpose of complying with specific, applicable federal, state or local law are NOT indicative of control
- But, acts of company that go beyond such compliance with law and instead serve the company's own compliance methods, standards, QC, or contractual or customer standards may suggest control
- More control suggests employee status; less control suggests IC status

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Factor 5: Extent to which work performed is integral part of employer's business

- Is the function the worker performs an integral part of the business? Is it critical, necessary or central to the business?
 - If yes, suggests employee status
 - If no, suggests IC status









- Worker does not use specialized skills or is dependent on training from potential employer = employee
- Worker brings specialized skills to the relationship (but does not use in connection with a "business-like initiative") = not itself indicative of IC status
- Worker brings specialized skills to the relationship + uses in connection with a "business-like initiative" = suggests IC status

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Application of factors



- No single factor or set of factors determinative
- Worker need not satisfy all of the factors to qualify as IC
- All factors are weighed to assess whether worker is economically dependent on company for work, according to totality of circumstances





• . . . of California/New Jersey/etc. fame

- Very difficult to satisfy
- IC status only proper where all three factors are present:
 - Worker free from control in performance of work
 - Work is outside usual course of company's business
 - Worker is customarily engaged in independent business of the same nature as involved in the work being performed

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Remember, there are lots of tests, and multi-state employers must consider state-specific standards







 Engage through third-party/staffing firm or worker's business entity if possible

- Do not use for routine work/integral business functions
- Avoid routine supervision, tracking, reporting requirements
- Focus on end results, not details of how work gets done

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Structuring to minimize risk (cont.)



Base pay on project/performance vs. time

- Require worker to supply own equipment and materials if feasible and consistent with security standards
- Avoid "look and smell" of employees (email addresses, attire, logos, ID badges, etc.)
- Do not include in employee meetings/functions





- Do not prohibit worker from working for others
- Require worker to have insurance and workers' comp coverage
- Use carefully drafted/legally reviewed agreement

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Resources

 https://www.dol.gov/agencies/whd/flsa/miscla ssification/rulemaking



"Everything old is new again."

- lots of people

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FLSA Refresher

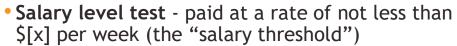
- Requires minimum wage and overtime, unless an exemption applies

- Exemptions:
 - Executive
 - Administrative
 - Professional
 - Highly-compensated employees
 - Computer employees
 - Outside sales

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- Salary basis test
 - Regularly receives predetermined amount of compensation each pay period on a weekly, or less frequent, basis
 - Subject to specific exceptions, cannot be reduced because of variations in quality or quantity of work
- Duties test

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Increase in salary threshold

- Effective July 1, 2024
- Additional salary threshold increases are scheduled for:
 - January 1, 2025
 - July 1, 2027
 - Every 3 years thereafter



Increases in salary threshold

DATE	STANDARD SALARY LEVEL	HCE ANNUAL COMPENSATION
Before July 1, 2024	\$684/week (\$35,568/year)	\$107,432 (including at least \$684/week on salary basis)
July 1, 2024	\$844/week (\$43,888/year)	\$132,964 (including at least \$844/week on salary basis)
January 1, 2025	\$1,128/week (\$58,656/year)	\$151,164 (including at least \$1,128/week on salary basis)
July 1, 2027 (and every 3 years thereafter)	To be determined	To be determined

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Bonuses, commissions, incentives

- Can count for up to 10% of salary level
 - Must be non-discretionary
 - May be paid annually "or more frequently"
 - "Catch-up" payment allowed
 - Can include all bonuses and other incentive compensation to meet HCE total annual compensation level





- Not to outside sales
- Not to learned professionals (lawyers, teachers, doctors)
- Not to computer professionals earning more than \$27.63 an hour

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Options for compliance

- Raise salary to meet new threshold
 - Ensure duties tests met
- Reclassify as non-exempt





- Remember "non-exempt" ≠ "hourly"
 - Can still pay a non-exempt employee a fixed salary for the week
 - Must satisfy minimum wage requirement
 - Must pay overtime for hours > 40 in workweek

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Options for compliance (reclassification)

- Convert to hourly
 - Reduce hourly rate to neutralize effect of OT
 - Formula: Weekly salary/(40+ (OT Hours x 1.5))
 - COMPLIANT NATIONALLY
- Convert to salaried non-exempt and pay overtime for hours over 40
 - OT rate is 1.5 times salary ÷ 40
 - Most expensive
 - Can reduce salary to neutralize the effect of OT
 - COMPLIANT NATIONALLY







- Fixed salary for fixed hours
 - Must have agreement
 - OT rate can change each week
 - NOT LEGAL IN ALL STATES
- Fluctuating workweek
 - Must have agreement
 - Straight time for all hours in workweek (at least Min. Wage)
 - Hours must fluctuate
 - NOT LEGAL IN ALL STATES

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Remember.....

- Give prior written notice of reduction/change in pay
- Specific requirements vary by state
 - NC: one full pay period in advance





- Policy should address if and when OT allowed
 - Advance authorization required?
 - Still have to pay OT if employee does not get approval
 - But may discipline employee if they violate the policy

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Tips for newly non-exempt employees

- Major concern "hidden" overtime
 - May be hard to predict overtime for formerly exempt employees
 - Employers need to look out for:
 - Accurate recordkeeping
 - Working through lunch
 - Working outside regular hours
 - Job-related "volunteer" work









- Decide whether to continue to pay to non-exempts
- If paid, OT calculation must include these payments
- Pay OT in same check as bonus, etc. is paid

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Tips for newly non-exempt employees

Discretionary Bonuses

- Employer must retain discretion over the fact that payment will be made AND the amount of the payment
- Not included in the regular rate of pay (no effect on employee's overtime compensation)

Nondiscretionary Bonuses

- Are typically made based on a prior contract, agreement, or promise to the employee
- Are included in regular rate of pay (increases employer's potential overtime liability)



Refresher on EAP duties tests - administrative





- Must be performance of office or non-manual work directly related to management or general business operations of employer or employer's customers, and
- Must include exercise of discretion and independent judgment with respect to matters of significance

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Functional areas for administrative exemption

- Tax
- Finance
- Accounting
- Budgeting
- Auditing
- Insurance

- Quality control
- Purchasing
- Procurement
 Advertising
 Marketing
- Research

Public

- Safety and health
- Personnel management
- resources Internet and
 Legal and

Human

- Employee benefits
- Labor relations
 - relations

- Government Computer relations
 - network
- database admin
- regulatory compliance
- "Similar activities"







 Primary duty must be managing the enterprise or customarily recognized department or subdivision

- Must customarily and regularly direct work of two or more other full-time employees (or equivalent)
- Must have authority to hire/fire or have recommendations as to hiring/firing/advancement be given particular weight

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Refresher on EAP duties tests - professional



- Learned professional
 - Primary duty must be performance of work requiring advanced knowledge (predominantly intellectual in character and requiring consistent use of discretion and judgment)
 - Advanced knowledge must be in field of science or learning, and acquired by prolonged course of specialized intellectual instruction





- Creative professional
 - Primary duty must be performance of work requiring invention, imagination, originality or talent
 - In a recognized field of artistic or creative endeavor

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Refresher on HCE exemption

- Highly compensated employees
- Must perform office/non-manual work
- Must meet enhanced salary level
- Must customarily and regularly perform at least one of the duties of an exempt EAP employee
- Not recognized in all states



Resources

 https://www.dol.gov/agencies/whd/overtime/rule making

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