

advisory

U.S. DEPARTMENT OF LABOR PROPOSES NEW RULE ON INDEPENDENT CONTRACTORS

On September 22, 2020 the U.S. Department of Labor (the “DOL”) released a proposed regulation addressing when a service provider should be classified as an independent contractor rather than an employee. The DOL is soliciting comments to the proposed new rules for a thirty (30) day period following publication in the Federal Register.



Background

For a variety of reasons, both employers and service providers may find it advantageous to characterize service providers as independent contractors rather than part-time, full time or temporary employees. From the putative employer’s perspective, the potential benefits include not having to withhold payroll taxes, pay for workers compensation insurance or include the “independent contractors” in health insurance, 401(k) or other employee benefit plans. From the service provider’s perspective, he or she receives the gross amount charged for services rendered, without reduction for payroll withholding taxes

and some expense that do not qualify as employee business expenses may become tax deductible on the service provider’s Form 1040, Schedule C.

Current Approach

The DOL’s current approach to determining a service provider’s status is based on an “economic reality” test. The test relies on seven (7) factors, none of which is determinative and all of which are given equal weight. In general terms, these are:

1. Are the services rendered an integral part of the principal’s business? (e.g., A painting contractor hiring a painter vs. hiring a computer repair person).
2. How much control does the principal have over the service provider’s work?
3. How much does the service provider have invested in facilities and equipment?
4. Does the service provider have an opportunity for profit or loss?
5. Does the service provider have an independent business organization and operation?
6. How permanent is the relationship?
7. Is the service provider in open market competition with others providing similar services?

Summary of Proposed New Rules

Although the “economic reality” test remains the principal focus of the proposed new rules, the seven (7) factor test summarized above would be replaced by two (2) “core” factors and three (3) “guidepost” factors. The first core factor is the principal’s control over the work. Has the principal contracted for an end-result or does the principal have substantial control over how the work is performed? The second core factor combines the opportunity for profit or loss, based on the service provider’s initiative, business acumen, etc., with the service provider’s investment in helpers, equipment and materials.

The core factors are given the most weight in the analysis but if they are not determinative or point to different conclusions, the guidepost factors come into play. These are (i) whether the work performed is part of an integrated unit of production; (ii) the permanence and likely duration of the relationship; and (iii) the amount of specialized training or skill required of the service provider that the principal does not provide.

The “integrated unit of production” may be the most important factor. For example: If a painting contractor hires a computer repair person, the relationship is more likely to be considered an independent contractor relationship than if a painting contractor hires a painter, whose services would be an integral part of the principal’s business.

Some Practical Advice

The proposed new rule is not yet final and may still be the subject of material changes. However, whatever form is finally adopted by the DOL, it is important to note that more strict state laws may still be applicable to businesses using service providers in a given state. Once the federal rules become effective, employers should review their independent contractor agreements to be sure they maximize the likelihood that their classification of service providers will be respected under both federal and applicable state laws. If you have questions about this issue or other business matters, please contact PLDO Partner William F. Miller at 508-420-7159 or email wmler@pdlolaw.com.



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