

Navigating the New Independent Contractor Rules: A Guide for Nonprofit Organizations



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Nonprofit organizations rely heavily on all sorts of workers, from full-time employees to volunteers to independent contractors. The U.S. Department of Labor recently finalized a new rule regarding the classification of workers that will impact how organizations designate workers as employees or independent contractors. The rule takes effect on March 11, 2024, and rescinds the 2021 independent contractor rule. This guide breaks down key elements of the rule and what nonprofits need to know.

The Purpose

The goal of the rule is to clarify the multifactor analysis used to determine whether a worker qualifies as an employee or an independent contractor under the Fair Labor Standards Act. This has implications for pay, benefits, tax status, legal protections, and more. The Department of Labor (DOL) aims to combat misclassifications that deprive workers of their rights and lets some organizations reduce labor costs unfairly.

6 Key Factors

The rule examines six key aspects of the worker's role and relationship to evaluate whether they are an employee or contractor:

1. **Opportunity for profit or loss** – Whether the worker has opportunities for profit or loss based on their management skills or business acumen. For example, an independent contractor typically can increase their earnings through their decisions, initiatives, or investments.
2. **Investment in work** – The degree of investment the worker makes, such as equipment, materials, employment of helpers, etc. An independent contractor often makes investments that support their business.
3. **Permanence of work relationship** – How permanent the work relationship is viewed by the parties. Independent contractors often work on a defined project or time period.
4. **Control over the work** – The nature and degree of employer control over the work, such as behavioral control, financial control, and relationship with pay. Employees are typically subject to greater control by the employer.
5. **Importance of work to the employer's business** – Whether the work is a key aspect of the employer's regular business. Work that is a core part of an employer's business is more likely to indicate an employment relationship.

6. **Skill and initiative of the worker** – The extent to which the worker uses specialized skills, exercises business judgment and works independently. Independent contractors typically have more autonomy and use independent judgment without close direction.

Call to Action

The consequences of misclassification can be great for both organizations and workers. In addition to direct financial costs, the cost in reputation could be devastating to a nonprofit organization dependent on contributions, grants, or membership fees. Therefore, nonprofits should proactively take steps to classify all workers appropriately under the law.

DOL does not explicitly call out specific common practices that would no longer be acceptable under the new rule. However, we can infer some practices that may need to change based on how the rule aligns classification guidance with longstanding legal precedent:

- Classifying workers as independent contractors solely because they have flexibility in when/where they work. Courts have said flexibility and control over one's schedule alone does not determine independent contractor status.
- Avoiding benefit costs by misclassifying employees as independent contractors. The rule aims to curb misclassification that appears to be motivated by avoiding overtime pay, unemployment insurance, etc.
- Dictating detailed requirements regarding how contractors must perform work. Courts view significant behavioral controls by the employer as indicative of an employment relationship.
- Classifying roles as contractors when the work is a core part of the business. Workers performing central business functions are more likely to be considered employees.
- Not allowing contractors autonomy over their profits/losses. Independent contractors typically have opportunities to earn and manage their own money.
- Automatically designating short-term, temporary, or gig workers as contractors. The duration alone does not determine classification.

Organizations should take action now to review current classifications for alignment with the new rule, consulting with an attorney or human resources professional as needed. Consider updating agreements and/or business practices like scheduling, supervision, pay, etc. to better align worker treatment with their classification. Take steps to convert improperly classified employees to employee status before **March 11, 2024**, and carefully plan communication with all impacted parties.

Looking Ahead

If an employee is misclassified as an independent contractor, the organization is vulnerable to lawsuits, regulatory actions, fines, and criminal charges for violating state and federal labor laws. Penalties can be substantial if it is determined that the individual, or group of individuals, was denied access to protections like minimum wage, overtime pay, unemployment insurance, workers' compensation, protection from discrimination, and other applicable benefits.

Although less likely, it is also possible for an independent contractor to be misclassified as an employee. In that scenario, the organization takes on unnecessary regulatory burdens and costs like payroll taxes, benefits, insurance, etc.

Regardless of the type of misclassification, reclassified workers are often unhappy with the change and frustrated by an insufficient explanation. Reclassification requires personal, sensitive communication and attention to the ongoing relationship between the worker and the organization. Framing the role the worker plays in advancing the mission of your organization can go a long way to securing a long-term and happy relationship.

While adapting this rule involves challenges, timely attention will pay off through ethical, lawful practices that support your people and your mission. For assistance in navigating the many business challenges facing your nonprofit organization, please contact [Kaydee Ruppert](mailto:Kaydee.Ruppert@deandorton.com), Associate Director at Dean Dorton: kruppert@deandorton.com or (859)425-7730.