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# LEGAL VIEW

## REAL ESTATE COMPANIES CAN REDUCE RISKS

### TIED TO INDEPENDENT CONTRACTOR CLASSIFICATION

**MISCLASSIFICATION OF WORKERS HAS** increasingly become a target of the U.S. Department of Labor, the National Labor Relations Board, and plaintiffs' attorneys who believe that many companies incorrectly use and identify employees as independent contractors. The real estate industry, particularly in the South, has been flagged by the Department of Labor, and the former head of the department's Wage and Hour Division has written that "the problem has long been entrenched" in the construction industry in particular.

Whether a regulator takes action or an independent contractor sues claiming to be misclassified, these cases pose significant risks for companies. In late 2023, two national companies paid \$55 million and \$30 million to settle misclassification claims. In most cases, the settlement is just the start of the impact to the bottom line: fees, penalties — including criminal penalties — are possible, and reclassifying independent contractors as employees results in substantial increases in labor expenses going forward.

These disputes are likely to continue to rise after the release earlier this year of the Department of Labor's final version of a new rule that is considered "employee-friendly" in how it approaches classification.

From our experience litigating these kinds of disputes and advising clients on independent contractor agreements, companies can take several steps to limit or avoid these types of

cases. They include ensuring use of clear and up-to-date contracts, as well as training employees at all levels of the company (top to bottom) on how to interact with independent contractors.

#### AN "EMPLOYEE-FRIENDLY" RULE ON INDEPENDENT CONTRACTOR CLASSIFICATION

**The Department of Labor's final rule, which took effect on March 11, may result in more independent contractors being classified as employees under the Fair Labor Standards Act.** In turn, that will increase compliance and cost burdens on companies — even those using legitimate independent contractors.

The rule replaced a 2021 rule that never went into effect, but that emphasized two factors in determining whether workers are employees: the nature and degree of control the workers had, as well as their opportunity for profit and loss. The 2024 rule focuses on six factors that "do not have a predetermined weight and are considered in view of the economic reality of the whole activity...." They are:

1. The worker's opportunity for profit or loss
2. The worker's financial stake and investment in the work
3. The degree of permanence of the work relationship
4. The degree of control the potential employer has

5. Whether the work is essential to the potential employer's business
6. The worker's skill and initiative

These factors should be familiar as they essentially reinstate the Obama-era "totality of the circumstances" rule. Examples of what will be considered include:

- Whether workers can determine or negotiate the pay or charge for work provided, or choose the time the work will be performed
- Whether investments are capital or entrepreneurial in nature or simply imposed unilaterally on workers
- Whether the relationship between the company and the worker is exclusive or whether the worker is engaged in projects for other companies
- Whether the worker maintains control over the method and manner of the work performed
- Whether the work is critical, necessary, or central to the potential employer's principal business.

It remains to be seen how these factors will continue to evolve in the courts, which is where they were initiated in the first place. But, we expect to see more cases brought by workers seeking to shift from the independent contractor column to that of an employee with the attendant benefits.

#### LESSONS LEARNED

So how can companies avoid such a monumental shift? Our experience tells

Do they permit loud laughing in Hawaii or just a low ha?

us that to come out ahead of this rule — and misclassification claims — companies need to do the work up front. It is critical to have contracts that clearly demonstrate — in words and actions — that workers are independent contractors. And, almost as importantly, to make sure everyone in the management chain understands the legal distinction and basis for it.

**When crafting contracts, it is important to understand that the test for independent contractor status also varies depending on which state you are in, and whether you are looking at classification under the FLSA, the Internal Revenue Code, the National Labor Relations Act, or ERISA.**

Thus, one size may not fit all. For a company working with a lot of independent contractors, looking at each contract anew can be time consuming and difficult, but the "bones" of the basic contract should be adaptable and flexible enough to address different issues appropriately in each signed agreement. Each agreement should also have a well-crafted arbitration clause consistent with cases in that area of the law, including language waiving class actions.

The contract is not the end of the story though. Courts look at the economic reality of the relationship, including the six factors the Department of Labor laid out in its "new" rule, and ask questions such as:

- Do the independent contractors control their own work environment?
- Can they hire people to work for them?
- Do they get to decide prices?

Not every answer has to be "yes" or "no" — but the totality must suggest that the worker is running their own business, not simply working for the company at issue.

Often, we see issues in litigation where a lower-level manager or new member of the team makes comments or behaves in a way that makes the relationship look more like an employee relationship. Thus, in addition to ensuring an up-to-date contract, it is important to train everyone who is

an employee — from senior managers to those on the front line — on what is required for non-employee workers to remain independent contractors. A simple example that has come up in court: senior managers telling independent contractors, "If you don't do what I'm asking, I'm going to fire you." That kind of language can provide a strong argument that a worker is really an employee and not "independent" at all.

Training employees on what it means to be an independent contractor — and how they should interact with independent contractors — is vital. Employees should have an arsenal of phrases such as: "You are an independent contractor, so you are able to make your own decision on that..." and they should repeat those phrases often so they stick in both the employees' and the independent contractors' minds.

### FINAL TAKEAWAY

Companies that win misclassification fights are the ones that have a clear internal understanding of their independent contractors' roles, that support their flexibility, and that avoid taking or exerting too much authority and control over them. Companies can accomplish these goals by investing on the front end to develop contracts and provide training on how the independent contractors should — and should not — be treated. ■

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## DIVERSIONS

### WORDS WITH NO ENGLISH EQUIVALENT

#### Schlemiel and schlimazel (Yiddish)

*[Remember the Laverne & Shirley theme song?]* Someone susceptible to bad luck. The schlemiel is the klutz who spills his coffee; the schlimazel is the one on whom it is spilled.

#### Backpfeifengesicht (German)

A face badly in need of a fist.

#### Kummerspeck (German) *[Literally: 'Griefbacon.']*

Excess weight gained from emotional overeating.

#### Cigil (Filipino)

The urge to pinch or squeeze something that is irresistibly cute.

**Tartle (Scottish)** The panicky hesitation right before you have to introduce someone whose name you can't remember.

#### Shemomedjamo (Georgian)

*[Literally: 'I accidentally ate the whole thing.']* When you're really full, but your meal is just so delicious, you can't stop eating.

**Mencolek (Indonesian)** When you tap someone lightly on the opposite shoulder from behind to fool them.

**Bakku-shan (Japanese)** The experience of seeing a woman who appears pretty from behind but not from the front.

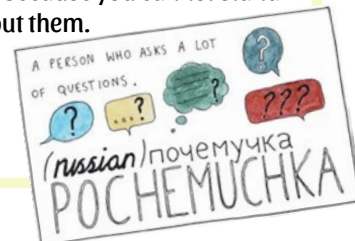
**Koi No Yokan (Japanese)** The sense upon first meeting a person that the two of you are going to fall in love.

**Zeg (Georgian)** The day after tomorrow.

**Cavoli Riscaldati (Italian) *[Literally: Reheated cabbage]*** The result of attempting to revive an unworkable relationship.

**Cafune (Brazilian Portuguese)** Tenderly running your fingers through your lover's hair.

**Ya'arburnee (Arabic) *[Literally: May you bury me.]*** The hopeful declaration that you will die before someone you love deeply, because you cannot stand to live without them.



Q: How many people are buried in the cemetery?

A: All of them.