

Independent Contractor vs. Employee

Did the DOL Make It Any Easier to Decide?

by Curtis D. Rostad

MOST EMPLOYERS ARE AT LEAST AWARE OF THE ISSUE of independent contractor versus employee. But making the determination has never been clear. In 2021, the U.S. Department of Labor announced a final rule clarifying the standard for independent contractor versus employee under the Fair Labor Standards Act (FLSA). That may sound encouraging, but it is doubtful that the actual rule and background information consisting of more than 1,200 pages makes the designation any easier. The rule only clarified the factors to consider that are still open to interpretation.

Why does this designation matter? There is a financial incentive to declare a worker an independent contractor. But declaring that designation does not make it so under the law. If a worker is deemed to be an independent contractor, the employer is not required to (1) pay either the minimum wage or overtime pay; (2) withhold income taxes; (3) pay FICA taxes; or (4) keep timecards or other records regarding the worker's activities. The employer's liability is limited. In addition, the employer does not have to provide workers' compensation or unemployment insurance coverage, health insurance, or other benefits employees may be entitled to.

Conversely, if an employer incorrectly classifies a worker as an independent contractor when that person should be classified as an employee, the employer would be liable for all these expenses plus possible enforcement action against them.

And just to make it more complex, since taxation is an issue here, the IRS has much to say on this subject. In fact, the IRS has its own checklist of generally overlapping questions to make this determination referred to as the 20 Factor Test. Yes, you have the possibility of *both* the Department of Labor *and* the IRS questioning the status of workers in your business. The employee can also file suit against an employer for incorrect classification.

In many cases, the designation is obvious:

- Suppose you need to have a toilet replaced and a sink leak fixed. You call

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Joe's Plumbing Shop. Joe comes out in his truck that even has his name on it. He brings in his tools and does the work. He hands you an invoice. You write him a check. He leaves and goes to his next job. This is his business. He is an independent contractor.

- You hire a full-time funeral director. That director works 40 hours a week (plus probably some overtime) for you. That director is entitled to the benefits you offer. That person is on the payroll and gets paid every two weeks. The funeral director is an employee.

We all know the difference even if we do not fully understand it. You might ask, how was that determination made? That is where this new rule comes in. We'll get to that.

The Economic Reality

In the final rule, the Department of Labor reaffirms an "economic reality" test to determine whether an individual is in business for themselves (independent contractor) or is economically dependent on an employer for work (an employee).

Returning to our example, the funeral director is dependent on you for their livelihood. The plumber has a business. The plumber might miss the revenue from your job but won't become homeless if you call another plumber.

The rule identifies and explains two "core factors" of whether a worker is economically dependent on someone else's business or is in business for themselves:

1. The nature and degree of control over the work. This factor weighs toward the individual being an independent contractor when the worker exercises substantial control over key aspects of the performance of the work, such as setting their own schedule and selecting their projects, or the ability to work for others, which might include the employer's competitors. This perfectly describes Joe the plumber.

In contrast, this factor weighs in favor of the individual being an employee when the employer exercises substantial control over performance of the work, such as controlling the individual's schedule or workload or by requiring the individual to work exclusively for the employer. This describes the funeral director.

Unfortunately, the term "this factor weighs" does not provide a definitive answer to the question. Imagine a scale with weights in the balance tilting to one designation or the other. That is how the determination is made. It's not a black or white issue.

2. The worker's opportunity for profit or loss based on initiative and/or

investment. This factor weighs toward the individual being an independent contractor when the worker has an opportunity to earn profits or incur losses based on the exercise of initiative or managerial skills. Again, this describes Joe the plumber. The number of customers he has, the quality of his work, and his business skill determines his financial reward.

This factor weighs toward the individual being an employee if the worker is unable to affect his or her earnings or is only able to do so by working faster or more hours. The employee funeral director is paid by the hour or a set salary (in some states) and generally does not earn more money by taking the initiative to do more tasks or do them better.

Additional Factors

The rule identifies three other factors that may serve as additional guideposts in the analysis.

1. The amount of skill required for the work. This factor weighs in favor of the individual being an independent contractor when the work requires specialized training or skill that the employer does not provide. This factor weighs in favor of the individual being an employee when the work requires no specialized training or skill; or the individual is dependent on the employer to equip them with the skills or training necessary to perform the job.

This factor may be confusing in our example because both jobs require specialized training. The difference here is that Joe the plumber already has all the skills he needs to perform the job. In fact, in most cases, the employer has no idea what needs to be done or how to do it. That is why you call Joe in the first place.

But while your funeral director has specialized training, that person is still dependent on you (especially in the case of an apprentice or newly licensed person) to provide additional training based on your own training and experience. The director

works under your guidance and direction; the plumber does not.

2. The degree of permanence of the working relationship between the worker and

the employer. This factor weighs in favor of the worker being an independent contractor if the work relationship is short in duration or sporadic. Joe the plumber does

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his job and goes on to the next one. He will come back the next time you have a plumbing problem—if and when he is available and if he wants to do your job.

This factor weighs in favor of the individual being an employee if the work relationship is intended to be indefinite in duration or continuous. Your funeral director reports for work every day and assuming you have a good working relationship, you both hope the work relationship lasts a long time.

3. Whether the work is part of an integrated unit of production. This factor weighs in favor of an individual being an independent contractor when the work is separate from the employer's production process.

This factor weighs in favor of the individual being an employee if the work is a component of the employer's production process for a good or service.

This one might also seem confusing:

- While having a working bathroom is important to your business, Joe the plumber has nothing to do with providing funeral services.
- Your funeral director/embalmer performs the essential services your firm provides to the families who call you.

Finally, other factors can be considered when making the contractor versus employee determination. The actual practice of the worker and the employer is more relevant than any contract that might exist or how things theoretically are to be done. For instance, the IRS and some court cases have considered other factors including who provided the tools and equipment necessary to do the job and whether the worker is able to engage others to assist.

Deathcare Staff: What About Me?

How do funeral homes and cemeteries potentially run afoul of the law? The Department of Labor or the IRS have audited funeral homes and claimed that musicians (and even ministers, especially if they are retired and are not providing funeral services as part of their church ministry) are employees rather than independent contractors. After all, there are factors that point in both directions:

- They do not operate their own music

business, but their schedule is set by the funeral home.

- The funeral home does not really exercise control over their work.
- They are free to work for any other funeral home.
- Their "employment" is sporadic and of short duration.

We can generally show that these individuals are not employees. Better yet, if you have the family pay the musician directly rather than as a cash advance, the issue becomes moot.

Using the Department of Labor criteria, let's consider more examples of situations that can arise in your business:

- What about part-time cemetery or funeral help and drivers? While their engagements might be sporadic, they anticipate an indefinite working relationship with your firm, and their work is directly controlled by the funeral director. Are they independent contractors or employees?
- What happens if one of those part-time employees is also a retired minister? Sometimes the minister helps direct funerals and sometimes officiates. Independent contractor or employee? Can the minister be both?
- Your funeral director is also an organist at their church. The family asks the director to play at a funeral. Are they doing so as an independent contractor or as your employee? Does it make a difference if they are using the instrument in your funeral home or that the service is held at the church?
- What about gravediggers at rural cemeteries? This might be an easy answer if the guy has an excavating business, but what if he is a farmer or rancher who happens to own a backhoe? Independent contractor or employee?
- If you own a cemetery, does the cemetery use a third party for gravedigging or installation of markers? Independent contractor or employee?
- You engage a college student to mow the lawn at the funeral home and shovel snow in the winter. Independent contractor or employee?
- It's easy to determine that an outside janitorial service is an independent

contractor. But what if one of your full-time employees and her husband come in after hours and clean the funeral home as a part-time job for both of them? Independent contractors or employees? And please note that since she is already an employee, if her janitorial work is as an employee, you will have to pay her time and a half for overtime.

- You have a retired embalmer living in town who embalms for you when you are busy. There is also a trade service in your area that you sometimes utilize. Does it make a difference if the embalming is done in your prep room or at the embalmer's own facility? Essentially, the same thing is being done. Are they independent contractors or employees?
- One funeral home used a trade embalmer who did all the preparation work in the funeral home. They used him so often they finally signed a contract with him to do all the embalming. Should he have been classified as an employee all along? Did that contract make him an employee? What if both parties to the contract specify that the worker is an independent contractor?

When faced with these conflicting factors and no clear guidelines, what should a funeral home or cemetery owner do? You have probably guessed that our advice is to talk to an accountant or attorney versed in employment law, or an HR specialist. The cost of doing so will clearly be less than the cost of making the wrong determination on your own. ❏



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