

OCTOBER 13, 2022 | WAGE & HOUR COMPLIANCE

New DOL Rule on Classifying Employees, Independent Contractors

On October 13, 2022, the Department of Labor (the "DOL") published its proposed rule on classifying employees and independent contractors. This rule would update the factors analyzed when determining whether a worker is an independent contractor or an employee under the Fair Labor Standards Act (the "FLSA").

DOL's press release revealed that when drafting this rule, it focused on preventing employee misclassification as independent contractors, preserving worker rights, and providing a consistent approach to resolving FLSA cases. Specifically, Secretary of Labor Marty Walsh said:

"While independent contractors have an important role in our economy, we have seen in many cases that employers misclassify their employees as independent contractors, particularly among our nation's most vulnerable workers... Misclassification deprives workers of their federal labor protections, including their right to be paid their full, legally earned wages. The Department of Labor remains committed to addressing the issue of misclassification."

Under the newly proposed rule, "an employer suffers or permits an individual to work as an employee if, as a matter of economic reality, the individual is economically dependent on that employer for work." The rule differentiates employees from independent contractors in stark terms – explaining that an independent contractor is only a worker who is "as a matter of economic reality, in business for themselves."

Notably, the rule sets forth a six-factor test to guide any assessment of the economic realities of the working relationship between a worker and an employer. Those six factors are:

- *Opportunity for profit or loss depending on managerial skill.*
 - Whether the worker exercises managerial skill that affects the worker's economic success or failure in performing the work.
- *Investment by the worker and the employer.*
 - Whether any investments by a worker are capital or entrepreneurial in nature.
- *Degree of permanence of the work relationship.*
 - This factor weighs in favor of the worker being an employee when the work relationship is indefinite in

duration or continuous, which is often the case in exclusive working relationships. This factor weighs in favor of the worker being an independent contractor when the work relationship is definite in duration.

- *Nature and degree of control.*
 - This factor considers the employer's control, including reserved control, over the performance of the work and the economic aspects of the working relationship.
- *Whether work performed is an "integral" part of the employer's business.*
 - This factor does not depend on whether any individual worker in particular is an integral part of the business, but rather whether the function they perform is an integral part
- *Skill and initiative.*
 - Whether the worker uses specialized skills to perform the work and whether those skills contribute to business-like initiative. Where the worker brings specialized skills to the work relationship, it is the worker's use of those specialized skills in connection with business-like initiative that indicates that the worker is an independent contractor.

This new rule is a departure from the prior approach indicated in DOL's 2021 Rule detailing how to analyze whether workers were independent contractors under the FLSA (the "2021 IC Rule."). That rule focused its analysis on two core factors — the nature and degree of control over the work, and the worker's opportunity for profit or loss (with much less weight given to three other factors: the amount of skill required for the work, the degree of permanence of the working relationship between the worker and the employer, and whether the work is part of an integrated unit of production).

The Department identified the 2021 IC Rule as a departure from the FLSA's text, purpose, and case law applying the economic realities test (a test that used a variety of factors to analyze whether a worker was economically dependent on the employer for work) before 2021.

Both the spirit and text of the new rule provide more opportunities for workers who might have previously been classified as independent contractors, to in the future be classified as employees. The rule accomplishes this by boosting the weight given to the degree of permanence of the working relationship between worker and employer, and the discussion of whether work performed is integral to the employer's business. Those two factors were previously lightly weighted in independent contractor analysis under the 2021 IC Rule.

The Department cited this departure as an additional reason for it proposing its 2022, affirming that "retaining the 2021 IC Rule would have a confusing and disruptive effect on workers and businesses alike due to its departure from case law describing and applying the multifactor economic reality test as a totality-of-the-circumstances test."

The proposed rule will be open for public comment for 45 days (until Monday, November 28, 2022).