CLIENT ALERT

'Most Workers Are Employees Under the FLSA': DOL Issues Guidance on Classifying Workers

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Shortly after announcing plans to more than double the base salary level required for exempt employees, the U.S. Department of Labor (DOL) is taking aim at what it claims is an increasing trend among U.S. businesses—misclassifying employees as independent contractors. DOL recently issued an Administrative Interpretation (AI) in which it left little doubt about its position, writing that "most workers are employees under the FLSA." The AI does not set forth any new standards, but it takes an aggressive, worker friendly approach to the "economic realities" test that courts use to determine whether particular workers are misclassified as independent contractors.

DOL's AI emphasizes that the "economic realities" test should be applied in a manner consistent with the FLSA's guidance that "the scope of the employment relationship is very broad." In particular, DOL emphasizes that the FLSA's definition of "employ" means to "suffer or permit to work" and was "specifically designed to ensure as broad of a scope of statutory coverage as possible." The DOL is thus reinforcing the presumption that an individual is an employee absent the employer's ability to demonstrate through the application of the economic realities factors that the he or she is properly classified as an independent contractor.

The AI then provides DOL's interpretation of the following six factors that courts consider in applying the "economic realities" test:

- Is the work an integral part of the employer's business?
- Does the worker's managerial skill affect the worker's opportunity for profit or loss?
- How does the worker's relative investment compare to the employer's investment?
- Does the work performed require special skill and initiative?
- Is the relationship between the worker and the employer permanent or indefinite?
- What is the nature and degree of the employer's control?

Although many courts in the past have focused on this last factor of "control," the AI specifically states that no factor is more important than any other. DOL argues that courts should consider all the factors equally in determining the ultimate question of whether the worker is economically dependent on the employer—and therefore an employee—or is instead truly in business for him or herself, and therefore an independent contractor.

The AI's discussion cites numerous judicial decisions to support its broad interpretation of the "economic realities" test. It also includes examples from industries in which DOL suggests there is systematic abuse of the independent contractor designation, including construction, health care, white collar freelancing situations, and miscellaneous service industries including janitorial workers and cable TV installers. The AI further cautions in a footnote that DOL will be on the lookout for fraud, specifically mentioning that its guidance also applies in relationships where workers have been encouraged or required by employers to set up their own separate corporations (or other contractual fictions) to avoid the requirements of an employment relationship.

Unlike DOL's recently proposed regulations regarding the salary level requirement, the AI is not subject to "notice and comment" rulemaking and therefore is effective immediately. Accordingly, the AI will not be entitled to the same level of deference from courts as traditional regulations promulgated under the Administrative Procedure Act. How courts react to DOL's guidance regarding the application of the "economic realities" test is an open question.

The AI serves as an important reminder that the consequences of misclassifying workers as independent contractors are significant. They include back payments for employer-side employment taxes, workers' compensation contributions, and unemployment insurance, as well as payments of employee benefits, overtime, and possible liabilities for failure to provide benefits under other employment statutes like the Family Medical Leave Act that borrow the FLSA's definition of employee.

The AI is yet another confirmation of the current regulatory push against various types of independent contractor arrangements. Employers are well-served by taking advantage of this type of regulatory guidance to review existing relationships with workers designated as consultants, freelancers and other sorts of independent contractors.

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