

Employee Benefit ■ Plan Review

U.S. Department of Labor Issues Proposed Rule on Independent Contractors

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The U.S. Department of Labor (DOL) has issued a proposed rule¹ that modifies the legal framework for determining whether a worker is an employee or independent contractor under the Fair Labor Standards Act (FLSA).

The proposed rule would rescind the current independent contractor rule² (adopted by the Trump Administration in 2021), which simplified the multi-factor test, and heavily weighted two “core” factors – workers’ control over their work and opportunity for profit or loss – in determining the status of workers. The new rule returns to a “totality-of-the-circumstances” analysis, which balances all factors equally. While the current rule is perceived as more favorable to respecting a worker’s independent contractor status, this shift in legal framework is expected to lead to more determinations that workers are employees, most particularly, gig workers.

DEFINITIONS

The proposed rule broadly defines an “employee” as any individual whom an employer “suffers, permits, or otherwise employs to work” and is intended to “encompass as employees all workers who, as a matter of economic reality, are economically dependent on an employer for work.”

In contrast, an “independent contractor” is a worker who is, “as a matter of economic

reality, in business for themself.” In doing so, the proposed rule clarifies that “[e]conomic dependence does not focus on the amount of income earned, or whether the worker has other income streams.”

“TOTALITY-OF-THE-CIRCUMSTANCES” ANALYSIS

The proposed rule would establish a non-exhaustive six-factor economic realities test; no one factor is dispositive. The factors include:

1. “*Opportunity for profit or loss depending on managerial skill.*” This factor considers whether the worker exercises managerial skill that affects the worker’s economic success or failure in performing the work.

The following facts, among others, may be relevant:

- Whether the worker determines or can meaningfully negotiate the charge or pay for the work provided;
- Whether the worker accepts or declines jobs or chooses the order and/or time in which the jobs are performed;
- Whether the worker engages in marketing, advertising, or other efforts to expand their business or secure more work; and

- Whether the worker makes decisions to hire others, purchase materials and equipment, and/or rent space.

If a worker has no opportunity for a profit or loss, then this factor suggests that the worker is an employee. Some decisions that affect the amount of pay a worker receives, such as working more hours or taking more jobs, are not indicators of exercising managerial skill under this factor.

2. *“Investments by the worker and the employer.”* This factor examines whether a worker’s investment is “capital or entrepreneurial in nature.” It also clarifies that costs borne by a worker to perform a job (e.g., tools and equipment) are not evidence of capital and entrepreneurial but instead indicate employee status. Additionally, a worker’s investment should be considered on a relative basis with the company’s investment in its overall business.
3. *“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 usually the case in exclusive working relationships. A work relationship that is definite in duration, non-exclusive, project-based, or sporadic, is evidence of independent contractor status. Seasonal or temporary nature of work or unique operational characteristics to certain industries alone are not, however, indicative of independent contractor status.
4. *“Nature and degree of control.”* This factor examines the company’s control, including reserved control, over the performance of the work and the economic aspects of the working relationship. Facts relevant

to the company’s control over the worker include whether the it sets the worker’s schedule, supervises the performance of the work, or explicitly limits the worker’s ability to work for others.

Additionally, facts relevant to the company’s control over the worker include whether the it uses technological means of supervision (such as by means of a device or electronically), reserves the right to supervise or discipline workers, or places demands on workers’ time that do not allow them to work for others or work when they choose.

Whether the company controls economic aspects of the working relationship should also be considered, including control over prices or rates for services and the marketing of the services or products provided by the worker. Control implemented by the company for purposes of complying with legal obligations, safety standards, or contractual or customer service standards may be indicative of control. More indicia of control by the company favors employee status; more indicia of control by the worker favors independent contractor status.

5. *“Extent to which the work performed is an integral part of the employer’s business.”* This factor considers whether the work performed is an integral part of the company’s business. It 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.

This factor weighs in favor of the worker being an independent contractor when the work they perform is not critical,

necessary, or central to the company’s principal business.

6. *“Skill and initiative.”* This factor examines whether the worker uses specialized skills to perform the work and whether those skills contribute to business-like initiative. Employee status is evidenced by a worker not using specialized skills in performing the work or a worker depending on training from the company to perform the work.

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.

BOTTOM LINE

The DOL’s proposed rule, if enacted in its current form, will likely have a significant impact on industries that rely on contract workers, particularly ride-share and food delivery companies. Under the proposed rule, many independent contractors would likely need to be considered for reclassification as employees, which would financially impact employers by way of employment taxes and workers’ entitlement to overtime pay, benefits, etc. 🌟

NOTES

1. <https://www.federalregister.gov/documents/2022/10/13/2022-21454/employee-or-independent-contractor-classification-under-the-fair-labor-standards-act>.
2. <https://www.federalregister.gov/documents/2021/01/07/2020-29274/independent-contractor-status-under-the-fair-labor-standards-act>.

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