

Employee or Independent Contractor? U.S. Department of Labor Changes the Standard

Labor & Employment Law Update

By Beverly Alfon on January 16, 2024

On January 10, 2024, the U.S. Department of Labor (DOL) published its Final Rule on the standard for determining who is an employee or independent contractor under the Fair Labor Standards Act (FLSA). The Final Rule is set to take effect on March 11, 2024.

Background

The FLSA provides wage and hour protections to “employees” that do not apply to “independent contractors,” including minimum wage and overtime minimums. Accordingly, misclassification of workers has been and continues to be a major focus of the DOL. In light of the potential economic impact that changes to standards used to determine worker classification can bring, it is matter of deep concern to businesses that classify workers as independent contractors.

The Final Rule rescinds the Trump administration’s independent contractor rule from 2021, which took a “core factors” approach to the analysis, giving heaviest weight to the factors of “the nature and degree of the individual’s control over the work” and “the individual’s opportunity for profit or loss.” Generally, the 2021 independent contractor rule was viewed as making it easier to classify workers as independent contractors.

The Final Rule

According to the DOL, the Final Rule returns to its prior guidance on independent contractor status and longstanding caselaw. The Final Rule returns to a “totality of the circumstances” analysis of “economic realities.” It states that the following six economic reality factors are to be applied equally, with no factors weighing heavier over the others:

1. **Opportunity for profit or loss depending on managerial skill.** This factor considers whether the worker has opportunities for profit or loss based on managerial skill (including initiative or business acumen or judgment) that affect the worker’s economic success or failure in performing the work. Does

the worker have the ability to accept or decline work as they choose? Does the worker engage in advertising or marketing to secure more work from others? Can the worker meaningfully negotiate the charge or pay for the work done?

2. **Investments by the worker and the potential employer.** This factor considers whether any of the worker's investments are capital or entrepreneurial in nature. Does the worker make investments in their ability to do different types of work or more work, reduce costs, or extend market reach? Is the worker making similar types of investments as the potential employer (even if on a smaller scale) to suggest that the worker is operating independently?
3. **Degree of permanence of the work relationship.** This factor focuses on whether the work relationship is indefinite in duration, continuous, or exclusive of work for other employers – or whether the relationship is for a certain period, non-exclusive, project-based, or sporadic based on the worker being in business for themselves, and marketing their services or product to different entities.
4. **Nature and degree of control.** This factor considers the potential employer's control, including reserved control, over the performance of the work and the economic aspects of the working relationship. Does the potential employer set the work schedule? Does the potential employer supervise the performance of the work or limit the worker's ability to work for others? Does the potential employer control economic aspects of the working relationship, such as control over prices and rates for services or products provided by the worker?
5. **Extent to which the work performed is an integral part of the potential employer's business.** This factor considers whether the work performed is an integral part of the potential employer's business. This factor is focused on whether the function the worker performs is an integral part of the business. If the work is critical, necessary, or central to the potential employer's principal business, it will weigh in favor of the worker being an employee.
6. **Skill and initiative.** This factor considers whether the worker uses specialized skills to perform the work and whether those skills contribute to business-like initiative. The worker's use of specialized skills in connection with business-like initiative will weigh towards the worker being an independent contractor.

These factors are not exhaustive and no single factor will determine a worker's status as an employee versus independent contractor. Rather, all of these factors are weighed to assess whether or not the work is economically dependent on the potential employer, under the totality of the circumstances.

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More to Consider

The Final Rule only sets the standard for determining a worker's status as an employee versus independent contractor under the FLSA. Different tests apply for determining a worker's classification under other laws, such as the Internal Revenue Code, National Labor Relations Act, Title VII of the Civil Rights Act of 1964, and state wage and hour laws.

Legal challenges to the Final Rule are expected. Republican members of the Senate Health, Education, Labor, and Pensions (HELP) Committee have already indicated that they will introduce a resolution to repeal the Final Rule under the Congressional Review Act. Business groups have also signaled their intent to challenge the rule in court.

What To Do Now

If your organization currently engages independent contractors, those business relationships should be evaluated under the Final Rule and all other applicable laws.

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