DOL Clarifies Who Is an Independent Contractor in Proposed Rule

By Allen Smith, J.D .

September 22, 2020

The U.S. Department of Labor (DOL) issued a proposed rule Sept. 22 to clarify when a worker is an employee covered by the Fair Labor Standards Act (FLSA) or an independent contractor. Independent contractors, including many gig-economy workers, are not eligible for minimum wage, overtime and other benefits that employees must receive. The proposed rule adopts an "economic reality" test to determine a worker's status as an FLSA employee or independent contractor.

"Businesses want clarity and specificity with respect to their engagement of independent workers. We are hopeful that this rule will help ensure that worker classifications are accurate, reflect today's modern workplace, and accommodate the needs of employers and workers alike," said Emily M. Dickens, the Society for Human Resource Management's (SHRM's) corporate secretary, chief of staff and head of Government Affairs. "SHRM looks forward to commenting on the proposed rule."

There will be a 30-day comment period after the proposed rule's official publication in the *Federal Register*.

The rule, if finalized as proposed, would make classifying workers as contractors easier, according to Rich Meneghello, an attorney with Fisher Phillips in Portland, Ore. But it

would not overturn worker-friendly state independent-contractor laws, such as the one in California, he added.

Economic Reality Test

Under the proposed economic reality test, the DOL would consider whether a worker is in business for himself or herself and thus is an independent contractor, or if the worker is economically dependent on an entity for work and is an employee.

In making this determination, the DOL would identify two core factors:

- The nature and degree of the worker's control over the work.
- The worker's opportunity for profit or loss based on initiative or investment.

It also would identify three other factors that may serve as additional guides in the analysis:

- The amount of skill required for the work.
- The degree of permanence of the working relationship between the worker and the potential employer.
- Whether the work is part of an integrated unit of production.

But the two core factors are entitled to greater weight than the other factors, the DOL noted.

Core Factors

The first factor—the nature and degree of the individual's control over the work—would suggest that an individual is an independent contractor to the extent that he or she exercises substantial control over key aspects of the performance of the work, the DOL explained.

Examples of an individual's substantial control include:

- Setting his or her own work schedule.
- Choosing assignments.
- Working with little or no supervision.
- Being able to work for others, including a potential employer's competitors.

In contrast, the control factor would weigh in favor of classification as an employee to the extent that a potential employer, rather than the individual, exercises substantial

control over key aspects of the work, including through requirements that the individual work for the employer exclusively during the working relationship.

The proposed rule clarifies that requiring an individual to comply with specific legal obligations, satisfy health and safety standards, carry insurance, meet contractually agreed-upon deadlines or quality control standards, or satisfy other similar terms that are typical of contractual relationships between businesses would not constitute control that makes the individual more or less likely to be an employee under the FLSA.

The second factor—the worker's opportunity for profit or loss based on initiative or investment—would, under the proposed rule, suggest that an individual is an independent contractor if he or she has an opportunity for profit or loss on either:

- The exercise of personal initiative, including managerial skill or business acumen.
- The management of investments in or capital expenditure on, for example, helpers, equipment or materials.

[Need help with legal questions? Check out the new SHRM LegalNetwork.]

Other Factors

As for the skill factor, the DOL proposed focusing on the amount of skill required. "The department believes that this approach would sharpen the distinction between the economic reality factors by focusing on skill, as opposed to aspects of control," the department said.

Because the worker's ability to work for others is already analyzed as part of the control factor, the proposed rule articulates the permanence factor without referring to the exclusivity of the relationship between the worker and potential employer.

The permanence factor would weigh in favor of an individual's being classified as an independent contractor when the working relationship is definite in duration or sporadic. By contrast, the factor would suggest someone is an employee if the working relationship is indefinite in duration or continuous.

The "integrated unit" factor would focus on whether an individual works in circumstances analogous to a production line. "This factor weighs in favor of employee status where a worker is a component of a potential employer's integrated production process, whether for goods or services," the DOL said. "The overall production process need not be a physical assembly line, but it must be an integrated process that requires the coordinated function of interdependent subparts working toward a specific unified

purpose." This may happen when the worker depends on the overall process to perform work duties, such as, for example, a programmer who works on a software development team.

Another example would be an individual who works closely by conceded employees and performs identical or closely interrelated tasks, such as where an individual provides office cleaning services as part of a team of employees.

But if the first two core factors—control and opportunity for profit or loss—point toward the same classification, their combined weight is substantially likely to outweigh the other factors, the DOL said.

Historically, whether the DOL considered someone to be an independent contractor was made by examining five or six factors. Now the factors other than the two core factors are secondary, said Josh Harrison, an attorney with Ogletree Deakins in Birmingham, Ala.

"Stakeholders should consider submitting comments to ensure they have a voice in shaping the final rule," said Susan Harthill, an attorney with Morgan Lewis in Washington, D.C.