U.S. DEPARTMENT OF LABOR PROPOSES NEW INDEPENDENT CONTRACTOR RULE FOR FEDERAL WAGE AND HOUR PURPOSES

Hodgson Russ Labor & Employment Alert
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On October 13, 2022, the United States Department of Labor ("DOL") published a Notice of Proposed Rulemaking ("NPRM") that would change the standard for determining whether a worker is an employee or an independent contractor under federal wage and hour law. This issue continues to be a political football, with the Obama, Trump, and now Biden administrations each proposing their independent contractor classification rule. The most recent proposal would return to a more labor-friendly standard and could make it harder for businesses to classify workers as independent contractors under the Fair Labor Standards Act ("FLSA").

Why does the proposed rule matter?

Under the FLSA, employees are entitled to certain benefits and protections, such as a minimum wage and overtime premiums. Independent contractors, however, are not entitled to those same benefits and protections. Many employers today, particularly in light of recent labor shortages and inflation, may consider hiring independent contractors rather than employees to save on wages, benefits, and other labor costs. However, employers should be wary of this approach and the ever-changing rules regarding the classification of independent contractors. Calling a worker as an independent contractor – and even entering into a contract that memorializes the independent contractor tutus – does not necessarily mean the worker will legally qualify as an independent contractor, and the so-called "misclassification" of independent contractors remains a significant risk for employers.

What is the current rule?

In the final days of the Trump administration, the DOL adopted a rule that was intended to make it easier for employers to classify workers as independent contractors under the FLSA. The rule identified five "economic reality" factors to determine whether a worker was an employee or independent contractor. The factors included the following:

1. The nature and degree of the individual's control over the work

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2. The individual's opportunity for profit or loss
3. The amount of skill required for the work
4. The degree of permanence of the working relationship
5. Whether the work is part of an integrated unit of production

The factors that carried the most weight in that analysis were the nature and degree of control over the work and the worker's opportunity for profit or loss. According to the Trump rule, if these two factors pointed toward the same classification, there was a "substantial likelihood" that such classification was the accurate one.

What is the proposed rule?

The proposed rule would rescind the Trump-era rule, and return to the Obama-era "economic dependence" approach, which assesses the degree to which the worker depends on the company for their economic survival. In conducting this analysis, courts look at the "totality of the circumstances" and consider six non-exhaustive factors. No single factor is dispositive and the weight given to each factor depends on the facts and circumstances of each particular case.

The factors include the following:

1. *Opportunity for profit or loss depending on managerial skill*

This factor considers whether the worker exercises his/her own managerial skill that affects his/her economic success or failure. For example, if the worker can (1) negotiate his/her pay; (2) accept or decline jobs; (3) choose the order and/or time in which the jobs are completed; and/or (4) make decisions to hire others and/or purchase materials and equipment, it is more likely that a court will consider a worker an independent contractor and not an employee.

2. *Investments by the worker and the employer*

This factor considers whether investments by a worker are capital or entrepreneurial in nature. For example, capital or entrepreneurial investments are indicative that a worker is an independent contractor, not an employee.

According to the NPRM, costs like tools, equipment to perform specific jobs, and the workers' labor are not, however, evidence of capital or entrepreneurial investments. Moreover, "[t]he use of a personal vehicle that the worker already owns to perform work— or that the worker leases as required by the employer to perform work—is generally not an investment that is capital or entrepreneurial in nature." This narrowing of the types of investments that reflect independent contractor status arguably makes the rule proposed by the Biden administration even more labor-friendly than the one adopted during the Obama administration.

3. *Degree of permanence of the work relationship*

This factor considers whether the work relationship between the employer and the worker is indefinite/continuous or definite/nonexclusive. For example, a worker may qualify as an independent contractor, and not an employee, where his/her work relationship is definite in duration, nonexclusive, project-based, or sporadic based.

4. *Nature and degree of control*

This factor considers whether the employer controls the performance of the work. The more control an employer has over the workers, the more likely that the worker is an employee and not an independent contractor. Courts consider the degree to which the employer: sets the worker's schedule; supervises the worker; limits the worker's ability to work for others; and/or disciplines the worker.

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 employer's business. If the worker is performing work that is critical, necessary, or central to the employer's principal business, it is more likely that the worker is an employee, not an independent contractor.

6. *Skill and initiative*

This factor considers whether the worker uses specialized skills to perform their work and whether those skills contribute to business-like initiative. If the worker brings his/her specialized skills to the work relationship, it is more likely that the worker is an employee, not an independent contractor.

What's next?

The public has 45 days, or until November 28, 2022, to submit comments on the NPRM. After the comment period closes, DOL will review the public comments and may modify the proposed rule or adopt the proposed rule as a final rule.

If enacted in its present form, the proposed rule will likely have a major impact on industries that rely heavily on contract workers. However, all employers should be mindful that this proposed rule addresses only the independent contractor classification under the FLSA. Tests that apply under other laws, such as federal and state tax laws and state wage and hour laws, may create additional risks for a business seeking to classify one or more workers as an independent contractor.

If you have any questions about the NPRM or independent contractor classification issues generally, please contact **Peter C. Godfrey** (716.848.1246), **John Godwin** (716.848.1357), **Kinsey O'Brien** (716.848.1287), **Charles H. Kaplan** (646.218.7513), or any other member of our **Labor & Employment Practice.**