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DOL Publishes Final Independent Contractor Rule

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On January 2, the U.S. Department of Labor (DOL) published a hotly anticipated final rule, which establishes a six-factor test for determining whether a worker is an employee or an independent contractor for purposes of coverage under the Fair Labor Standards Act (FLSA). The final rule was adopted after publication of a proposed rule in October 2022 and following a 61-day comment period in which the DOL received more than 55,000 comments. The final rule also rescinds an independent contractor rule, issued in January 2021, which never went into effect due to legal challenges. The new final rule becomes effective on March 11.

Overview

Until 2021, neither the FLSA nor DOL regulations provided a definition of an "independent contractor" who would not be subject to the minimum wage, overtime, and other provisions of the FLSA. However, federal courts developed a body of case law, which took a holistic, fact-intensive approach. Throughout the 330-page preamble to the final rule, the DOL repeatedly emphasized that the final rule is intended to comply with, not change, that established case law.

As noted above, the final rule also rescinds a Trump administration independent contractor rule issued in January 2021, which never fully became effective due to legal challenges. The DOL's position is that the January 2021 rule impermissibly narrowed the factors that should be considered when making independent contractor classification determinations and improperly weighted certain factors over others.

The Economic Realities Test

The new final rule establishes a six-factor "economic reality" test, which the DOL says should be used to determine whether the worker is "economically dependent on the potential employer for work or is in business for themself." Those factors are:

1. Opportunity for profit or loss depending on managerial skill.
   Relevant facts here include whether the worker determines or can meaningfully negotiate the charge or pay for the work provided; whether the worker can accept or decline jobs; whether the worker chooses the order and/or time in which jobs are performed; whether the worker engages in marketing, advertising, etc. to expand their business; and other similar factors. Workers who behave more like their own managers will be more likely to be considered independent contractors.

2. Investments by the worker and the potential employer.
   For this factor, a court should consider the investments of the worker and the potential employer *on a relative*

basis, meaning that if a worker and the potential employer make similar types of investments in their own respective businesses, (including investments such as those which increase the workers' ability to do different types of or more work, reduce costs, or extend market reach), but the worker makes them on a smaller scale due to the smaller size of their business, the factor still weighs in favor of independent contractor status.

3. Degree of permanence of the work relationship.
   If the work relationship is indefinite, continuous, or exclusive of work for other employers, this factor weighs in favor of the worker being an employee. With respect to exclusivity, the DOL notes that many workers (who are properly classified as employees) might work for multiple employers due to economic need, while some workers (who are properly classified as independent contractors) may choose to work for a single person or entity because of a favorable business relationship. Therefore, the exclusivity of the relationship should be considered in light of the other factors in this test to determine whether the worker is in business for themselves or for the potential employer.

4. Nature and degree of control.
   This factor includes considerations, such as whether the potential employer sets the worker's schedule, supervises the performance of the work, or reserves the right to supervise or discipline the worker(s). This does **not** include actions taken by the potential employer for the sole purpose of complying with a specific law or regulation; however, if the potential employer requires the worker to comply with additional rules or policies, the worker is more likely to be an employee. For example, a company does not exercise control under this factor if it requires workers on its construction site to wear a hard hat as required by a city ordinance. However, it may exercise control if it requires those workers to attend weekly briefings, at a specific time and place, on the employer's safety policies and procedures.

5. Extent to which the work performed is an integral part of the business.
   This factor does not focus on whether the individual employee is integral to the potential employer's business, but rather whether the job they perform is critical, necessary, or central to that business. For example, if a potential employer's primary business is to make widgets, the workers who are involved in making those widgets (*i.e.*, on the production line, quality control, etc.) are performing work that is integral to the potential employer's business, and thus are more likely to be employees.

6. Skill and initiative.
   If the worker uses specialized skills to perform the work **and** uses those specialized skills in connection with initiatives to promote their own business, as opposed to the business of the employer, this factor weighs in favor of independent contractor status. Specialized skill alone does not support an inference that the worker is an independent contractor. Similarly, if the worker does not use their specialized skills to perform the work, or if the worker is dependent on training from the potential employer to perform the work, this factor weighs in favor of finding that the worker is an employee.

In addition to the above six factors, the DOL left the door open to consider additional factors on a case-by-case basis. The final rule indicates that "[a]dditional factors may be relevant … if [they] in some way indicate whether the worker is in business for themself, as opposed to being economically dependent on the potential employer for work." § 795.110(b)(7). It is not clear what those additional factors might be, but the rule provides for the

possibility that some other factors might lend themselves to determining that a worker is an independent contractor.

Effect on Employers

Because the final rule is intended to codify existing case law, rather than to change it, many companies will not be significantly affected by the rule. If an employer previously relied on the January 2021 rule, which was considered more independent contractor-friendly, the company should consult with trusted employment counsel to re-evaluate any independent contractor classifications, using the guidelines in the new final rule, in order to ensure ongoing compliance.

Additionally, companies should be mindful of applicable state law, particularly in the 28 states that have adopted the more stringent “ABC” test, and the additional eight that use some variation of the “ABC” test. In California, the “B” in the “ABC” test requires that the worker perform work, which is outside the employer’s usual course of business — otherwise, the worker is an employee.

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