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Labor & Employment CLIENT BULLETIN

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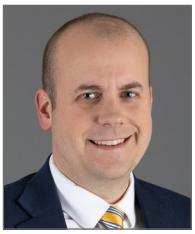

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As a reminder, this Advisory is being sent to draw your attention to issues and is not to replace legal counseling.

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Clarifying Employee and Independent Contractor Status Under the Fair Labor Standards Act

On September 22, 2020, the Department of Labor ("DOL") released a proposed rule providing a more employer-friendly interpretation of independent contractor status under the Fair Labor Standards Act.

The proposed rule provides a framework for classifying a worker as an independent contractor rather than an employee. Adopting a modified "economic reality" test, the proposed rule considers two core factors and three other "guideposts" to determine status. Under the two core factors, the DOL considers: (1) the nature and degree of the worker's control over the work and (2) the worker's opportunity for profit or loss based on personal initiative or investment. When the two core factors conflict, the three other factors serve as additional guideposts in the analysis, which assess: (3) the amount of skill required for the work, (4) the degree of permanence in the working relationship, and (5) whether the work is part of an integrated unit of production.

In shaping the analysis, the DOL advises that reality is more relevant than what may be contractually or theoretically possible when determining whether a worker is an employee or an independent contractor. Explaining the proposed rule, DOL Secretary Eugene Scalia stated that "[p]art of what's notable about this proposed rule is simply that we're doing it. In the more than 80 years since enactment of the Fair Labor Standards Act, or FLSA, the Department has never adopted a rule defining the term for general industry." Further, the DOL's stated purpose of proposing the regulation is to, "…explain the contours of the economic reality test and clarifies and sharpens a test that has become less clear and consistent through decades of case-by-case administration in the court of appeals. If the proposed rule were finalized, it would contain the Department's sole and authoritative interpretation of independent contractor status under the FLSA."

Prior to the proposed rule, previous administrations actively enforced misclassifications but did not pursue a regulation. Instead, employers were left to interpret the administrator interpretations related to the DOL's position on independent contractor classification, which effectively expanded the scope of liability for employers. Previous DOL guidance, citing appellate case law, discussed a six-factor economic realities test which the DOL interpreted as providing broad, employee-friendly coverage. Additionally, the DOL had explained that the "control" factor should not be given "undue weight" in considering the employment status. Here is how the DOL's position will effectively change via the proposed rule:

Old Test	New Test
Step One	
The DOL considers six "economic realities factors" in the context of the FLSA broad definition of "employ," meaning "to suffer or permit to work." Notably, no one factor was entitled to greater weight than another.	The proposed rule improves the certainty and predictability of the economic reality test by focuses on two core factors. If both core factors align, the analysis is complete.
1. The degree of control exercised or retained by the employer; 2. The worker's opportunity for profit or loss depending on his or her managerial skill; 3. The extent of the relative investments of the employer and workers; 4. Whether the work performed required special skills and initiative; 5. The permanency of the relationship; and 6. The extent to which the work performed is an integral part of the employee's business .	1. The nature and degree of the worker's control over the work; and 2. The worker's opportunity for profit or loss.
Step Two	
N/A	3. The amount of skill required for the work 4. The degree of permanence of the working relationship between the individual and the potential employer; and 5. Whether the work is part of an integrated unit of production

Although the DOL withdrew the administrator interpretations on June 7, 2017, the withdrawal did not change the legal responsibilities of employers under the FLSA and employers were still bound by existing case law relating to independent contractors. To fill this gap, the new proposal - focusing on the two core factors instead of six - should result in a consistent DOL position regarding which factors to weigh more heavily. In short, the two core factors in the proposed rule drive at the heart of the economic dependence question because they bear a causal relationship with the ultimate inquiry and should provide an easier analysis for employers when confronted with the independent contractor issue.

Additionally, the proposed rules should provide clarity and consistency in determining who is an employee or an independent contract while helping employers avoid unnecessary risks. The risks of misclassification can be high, including violations of wage and hours laws; unpaid income tax withholdings and Social Security, Medicare and unemployment insurance contributions; and gaps in workers' compensation insurance coverage. Such violations could potentially trigger liability for back wages, back benefits, liquidated damages, back payroll taxes, civil penalties, employee attorney's fees, employee litigation costs, and punitive damages.

The DOL has placed the proposed regulation on a fast-track, with the hope to finalize the rule before the end of 2020. Regardless of the new regulation, it is imperative that each employer look to their own state for guidance, as the DOL is just one of the many different agencies which evaluate independent contractor issues.

Additional Information

For more information, contact a member of Benesch's Labor & Employment Practice Group.

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