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DOL Proposes Delaying Newly Published Rule on Independent Contractors

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Employers may be disappointed to learn that the Department of Labor's recently issued rule clarifying the definition of "independent contractor" will likely no longer go into effect on March 8th, 2021. On January 20th, the White House issued a regulatory freeze halting all executive agencies, including the Department of Labor (DOL), from proposing or issuing any rule until the new administration reviews and approves it. Moreover, agencies are to "consider postponing" by 60 days the effective dates for any rules published in the Federal Register that have not yet taken effect.

On February 5, the DOL proposed to delay the effective date of its new rule from March 8th, 2021 to May 7, 2021. The delay would allow an additional opportunity for the DOL to review and consider the legal, policy, and enforcement implications of adopting the new legal standard for determining independent contractor status under the Fair Labor Standards Act (FLSA). Such implications include whether the rule effectuates the FLSA's purpose to broadly cover workers as employees, the costs and benefits attributed to the rule, including the assertion that workers as a whole will benefit from the rule, and whether the rule's explanation of the standard provides clarity for stakeholders and for the purposes of enforcement as was intended. The DOL has not stated that the postponement will result in an additional comment period on the substance of the rule. Comments are, however, currently being accepted on the proposal to delay the rule's effective date.

As issued on January 7th, the new rule itself provides clarity for employers on the classification of workers as employees or independent contractors. This is an important distinction under the FLSA, which sets forth a number of requirements that employers must adhere to for employees, but not for independent contractors, such as minimum wage and overtime pay requirements. Equally important, employees have rights against discrimination under Title VII, the ADEA, the ADA, and other statutes, that independent contractors do not enjoy. And employees have rights to employee benefits from which independent contractors may be excluded.

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The new rule adopts the "economic reality" test. Under the test, "[a]n individual is an independent contractor if the individual is, as a matter of economic reality, in business for him- or herself." Helpfully, the rule provides five factors (largely drawn from prior caselaw) to guide the ultimate classification:

(1) The nature and degree of the worker's control over the work;
(2) the worker's opportunity for profit or loss based on initiative, investment, or both;
(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.

Until the new rule takes effect, employers will have to rely on the existing law distinguishing employees from independent contractors. Current DOL guidance on the issue suggests analyzing seven factors: (1) the extent to which the services rendered are an integral part of the principal's business; (2) the permanency of the relationship; (3) the amount of the alleged contractor's investment in facilities and equipment; (4) the nature and degree of control by the principal; (5) the alleged contractor's opportunities for profit and loss; (6) the amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor; (7) the degree of independent business organization and operation. Although this test overlaps significantly with the economic reality test in the DOL's new rule, the current analysis requires a more exhaustive consideration of factors. Moreover, the old guidance is silent on which factors carry weight in the analysis. Helpfully, the new rule clarifies that the first two factors of the economic reality test are the most important. The new rule would therefore have made it a bit easier for employers to accurately distinguish independent contractors from employees.

Given the proposed delay of the DOL's new rule, employers should review the existing law on independent contractors to minimize the risk of misclassification liability. Employers must also keep in mind that state law may be more protective of workers than federal law. Connecticut, for example, utilizes a test (the "ABC" test) that treats more workers as employees than either the existing federal guidance or the (issued, but delayed) new federal rule, and employers who misclassify employees under state law may be liable for significant damages as a result.

For more information on this subject, or assistance with compliance review, contact any of the attorneys in our Labor, Employment, and Employee Benefits group.

Tags: Americans with Disabilities Act (ADA), Fair Labor Standards Act (FLSA), Independent Contractor, Title VII, U.S. Department of Labor