U.S. Department of Labor Issues New Worker Classification Regulations

January 15, 2021

Key Points:

- The DOL has issued new regulations setting forth the test to determine whether an individual is an independent contractor or an employee under the FLSA.
- Under the regulations, the "ultimate inquiry" is whether, as a matter of economic reality, the worker is economically dependent on the potential employer for work. The regulations provide a non-exhaustive list of factors that should guide the determination of whether a worker is an employee. For the DOL, the two most probative factors in the test are (i) the nature and degree of control over the work and (ii) the worker's opportunity for profit or loss based on initiative or investment.
- The regulations are consistent with FLSA case law in most respects. However, more controversial aspects of the regulations, including the DOL's view that the actual practices of a worker and a potential employer are more relevant to the analysis than either's contractual or theoretical rights, could prompt the new administration to withdraw the regulations—or Congress to intervene—before the regulations take effect on March 8, 2021.

On January 7, 2021, the U.S. Department of Labor (DOL) published a Final Rule containing a multifactor test for determining whether workers are independent contractors or employees. The regulations are published in a new Part 795 of 29 C.F.R. chapter V (see 20 C.F.R. ¶¶ 795.100–120) and take effect on March 8, 2021. The regulations will guide the DOL's enforcement of the Fair Labor Standards Act (FLSA) and are intended to be used by workers, employers and courts in classifying workers. If a worker is deemed to be an independent contractor, the business for which it performs work does not have to pay the worker minimum wage or overtime compensation under the FLSA.

The test evaluates the "economic reality" of the working relationship at issue, i.e., whether the worker is, as a matter of economic reality, in business for him- or herself as opposed to being economically dependent on the potential employer for work. The test identifies two "core factors" that, according to the DOL, are most probative of the question of whether a worker is economically dependent on someone else's business or in business for him- or herself: (i) the nature and degree of control over the work

Contact Information

If you have any questions concerning this alert, please contact:

Nathan J. Oleson
Partner
noleson@akingump.com
Washington, D.C.
+1 202.887.4425

Brian Glenn Patterson
Partner
bpatterson@akingump.com
Houston
+1 713.250.2214

Joshua Keith Sekoski
Counsel
jsekoski@akingump.com
Washington, D.C.
+1 202.887.4544

Courtney L. Stahl
Counsel
cstahl@akingump.com
Houston
+1 713.250.2140

Zara H. Shore
Associate
zshore@akingump.com
Washington, D.C.
+1 202.887.4583

and (ii) the worker's opportunity for profit or loss based on the worker's initiative or investment. Per the DOL, these factors each carry greater weight in the analysis than any other factor. If they both suggest the same classification, then the DOL will conclude that such classification is likely correct.

- **Nature and degree of control over the work.** Under the regulations, the nature and degree of control over the work weighs toward independent contractor status to the extent that the worker exercises substantial control over key aspects of the performance of the work, such as by setting his or her schedule, by selecting his or her projects or through the ability to work for others. By contrast, this factor weighs in favor of an employment relationship if the potential employer exercises such control, such as by setting the worker's schedule or by directly or indirectly requiring the worker to work exclusively for the potential employer. Requiring the worker 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 terms typical of contractual relationships between businesses, will not be held by the DOL to constitute control indicating an employment relationship.
- **The worker's opportunity for profit or loss.** In evaluating an individual's opportunity for profit or loss, the DOL will consider a worker's exercise of initiative or management of his or her investment in, or capital expenditure on, expenses intended to further his or her work, including, for example, helpers, equipment or material. The DOL will weigh the factor as favoring an employment relationship to the extent that the worker is unable to affect his or her earnings other than by working more hours or faster.

The DOL identified three additional factors that may serve as further guideposts in this analysis, particularly when the first two factors do not clearly point to the same classification: (iii) the amount of skill required for the work, (iv) the degree of permanence of the working relationship between the worker and the potential employer, and (v) whether the work is part of an integrated unit of production.

- **The degree of permanence of the working relationship.** The DOL will treat a work relationship definite in duration or sporadic as indicating independent contractor status, though seasonal work would not necessarily indicate such a classification. By contrast, this factor favors employee status where the work relationship is by design indefinite in duration or continuous.
- **Whether the work is part of an integrated unit of production.** The DOL will view this factor as favoring employee status to the extent that the worker's work is a component of the potential employer's "integrated production process for a good or service." If the work is segregable from the employer's production process, the factor will favor independent contractor status. The DOL will view this factor as different from the concept of importance or centrality of the worker's work to the potential employer's business. The DOL provides an example of a journalist who writes for a newspaper on a freelance basis and submits articles once every two to three weeks which may be rejected by the paper, but who does not communicate or work with the newspaper's employees other than its editor or assign or review articles. The DOL would view these facts as favoring independent contractor status because the journalist is not part of an integrated unit of production of the newspaper even though the writing of articles is an important part of producing newspapers. The location where the journalist works would not strongly indicate

either status since the DOL would view the physical location where his work is performed as largely irrelevant.

The DOL may consider other factors not listed in the regulations but only if they in some way indicate whether the worker is in business for him- or herself as opposed to being economically dependent on the potential employer for work.

One of the more controversial regulations states that the actual practices of the worker and potential employer are more relevant to the DOL's test than their respective contractual rights or what control the potential employer may theoretically exert. For example, the DOL will view a worker's theoretical ability to negotiate prices or work for competing businesses as less meaningful if the worker is prevented from exercising such rights. Likewise, the DOL may give a potential employer's contractual authority to supervise or discipline a worker less weight if the potential employer never exercises this authority. This interpretation of the FLSA may be interpreted as at odds with case law precedent in a number of jurisdictions holding that an employer's **right** to control the manner and means of a worker's work is probative of employment status.[1]

In the regulations, the DOL provides several hypothetical examples in which it applies the above factors, emphasizing that neither measures implemented by a potential employer in order to comply with specific legal obligations nor a great disparity in investment between a worker and potential employer that is irrelevant to the worker's opportunity for profit or loss would indicate employment status. However, performance of the same work as that performed by employees of a potential employer, in coordination with those employees, would favor employee status.

The future of the Final Rule is uncertain for several reasons. The Biden administration is expected to issue a directive to all agencies to delay the effective date of any pending regulation. During this period, the Biden administration could rescind this rule and propose another, or Congress could pass a joint resolution disapproving of the rule under the Congressional Review Act (CRA). Enactment of a resolution under the CRA would take the rule out of effect or prevent it from going into effect, and the agency would be prohibited from issuing a rule that is "substantially the same" without further authorization from Congress.

[1] See, e.g., *Razak v. Uber Techs., Inc*., 951 F.3d 137, 142 (3d Cir. 2020); *Keller v. Miri Microsys. LLC*, 781 F.3d 799, 807 (6th Cir. 2015); *Real v. Driscoll Strawberry Assocs., Inc*., 603 F.2d 748, 754 (9th Cir. 1979).

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