

Who is an Independent Contractor? DOL Issues New Rule

January 23, 2024

The issue of who is an independent contractor can be tricky, particularly in the age of technology. If an employer misclassifies an individual as an independent contractor, there are a number of penalties for which the employer could be held liable. Such penalties could include additional taxes and FICA contributions, back pay and legal fees for the misclassified worker, and fines up to \$10,000 per misclassified worker. Employers can even potentially be imprisoned for up to one year!

Who Is an Employee?

The [definition of employee](#) under the Fair Labor Standards Act (FLSA) is very circular. An employee is defined as “any individual employed by an employer.” An employer is defined as “any person acting directly or indirectly in the interest of an employer in relation to an employee.” The FLSA clearly does not cover independent contractors; however, the statute does not provide a definition for independent contractors either.

The 2021 Rule

In 2021, the Department of Labor (DOL) published regulations setting forth the test for determining who is an independent contractor. These regulations were controversial. While the DOL states that the purpose of the 2021 Rule was to “streamline” the economic reality test, the test was confusing to most – including the courts.

Under the 2021 Rule, the DOL defined five factors to consider when determining independent contractor status:

1. Nature and degree of control over the work.
2. Worker’s opportunity for profit or loss.
3. Amount of skill required for the work.
4. Degree of permanence of the working relationship between the worker and the employer.
5. Whether the work was part of an integrated unit of production.

While the 2021 Rule stated that the factors were not exhaustive and no one factor was dispositive, it emphasized the first two factors and called them “core factors.” The 2021 Rule provided that if both of the “core” factors indicate the same classification, as either an employee or independent contractor, there was a “substantial likelihood” that the indicated classification was the worker’s correct classification. Essentially, the three “non-core” factors were rarely considered.

Why the Change?

The DOL felt that the 2021 Rule did not fully comport with the FLSA's text and purpose and the court decisions addressing the issue. The DOL also felt that it did not address the modern economy, particularly in the age of app-based technologies.

The New 2024 Rule

The 2024 Rule states that economic dependence is the ultimate inquiry. Thus, an employee is someone who, as a matter of economic reality, is economically dependent on an employer for work. Considering economic dependence is in line with the DOL's longstanding position on how to distinguish between an employee and an independent contractor. The 2024 Rule sets forth the factors that should be used in establishing economic dependence.

The 2024 Rule does not use "core factors" and returns to the totality-of-the-circumstances analysis of the economic reality test. Thus, each factor stands on its own, and no one factor has a predetermined weight. The factors include:

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

In determining whether an individual has the opportunity for profit or loss depending on managerial skills, the DOL will look to whether the worker determines or can meaningfully negotiate the charge or pay for the work provided. Further, it will consider if the worker can decline jobs or can choose the order and time by which the jobs are performed. Additionally, the DOL will consider if the worker engages in marketing and is attempting to expand the business. Finally, it will consider if the worker makes hiring decisions, purchases materials and equipment, and/or rents space.

2. Investments by the worker and the potential employer.

In looking at investments, the DOL will consider if any investments by a worker are capital or entrepreneurial in nature. Costs such as purchasing worker tools and necessary equipment, labor costs, and costs that the potential employer poses on the worker are evidence of capital or entrepreneurial investments.

3. Degree of permanence of the work relationship.

If the relationship between the potential employer and worker is indefinite in duration, continuous, or exclusive of work for other employees, the worker is likely an employee.

4. Nature and degree of control.

The DOL will consider the potential employer's control, including reserved control, over the performance of the work and the economic aspects of the working relationship. The DOL will look to whether the potential employer sets the work schedule, supervises work, or otherwise limits the worker's ability to work for others. Control will not be found, however, when the potential employer demands that the work abide by regulations imposed by OSHA and any other applicable law.

5. Extent to which the work performed is an integral part of the employer's business.

In determining this factor, the DOL will not consider whether the worker is an integral part of the business but rather whether the function that the worker performs is an integral part of the business. An employee will be found to be an employee and not an independent contractor if the work being performed is critical, necessary, or central to the potential employer's principal business.

6. Skill and initiative.

The DOL will consider whether the worker uses any specialized skill to perform the work and whether the skills contribute to the business-like initiative. If the worker obtains skills from training provided by the potential employer, the individual will not be an independent contractor.

7. Any other factors that might indicate whether an individual is economically dependent on the employer for work.

The Takeaway

The new 2024 Rule is clearly more in line with the court decisions defining who is an independent contractor. Hopefully, we will have consistency between the DOL and the courts in tackling this thorny issue.

As always, please reach out to the author or any member of [McGlinchey's labor and employment team](#) if you have any questions.

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