PUBLICATION

To Be or Not to Be: Department of Labor Proposes Rule Addressing Employee/Independent Contractor Classifications

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Notice: The U.S. Department of Labor has extended the comment period related to this Proposed Rule, from November 28 to December 13, 2022. The Department has said it "takes seriously its obligation to consider any 'written data, views, or arguments' submitted by commenters and looks forward to reviewing all feedback . . . ." Should you or your company wish to submit comments to the Proposed Rule during this extended period, please contact the authors or a member of Baker Donelson's Labor & Employment Group.

On October 11, 2022, the U.S. Department of Labor announced that it will publish a Notice of Proposed Rulemaking in the Federal Register on October 13 to provide guidance on classifying workers as employees or independent contractors. With this Notice of Proposed Rulemaking, "the Department [of Labor] describes the economic reality factors that reflect the totality-of-the-circumstances approach that courts have taken for decades."

The Proposed Rule attempts to "restore the multifactor, totality-of-the-circumstances analysis to determine whether a worker is an employee or an independent contractor" under the federal Fair Labor Standards Act, that governs how employees are paid. Significantly, the Proposed Rule is not an adoption of the so-called "ABC Test" adopted by California and in variations by several other states, which is an extremely narrow test that results in most workers being classified as an employee. Rather, the "totality of the circumstances" standard in the Proposed Rule means that the DOL and courts have the ability to consider and apply different weight to a number of factors articulated in the Proposed Rule, and other factors deemed relevant to the analysis. This, on the whole, means the Proposed Rule provides far more flexibility for employers than the ABC Test and its variations.

For those hoping that the DOL would issue a clear, bright-line test that employers could apply to easily determine whether a worker is an independent contractor or an employee, this Proposed Rule does not meet the bill. What it lacks in certainty, however, is made up for in flexibility. The Proposed Rule necessarily allows the many different workplace scenarios and individualized circumstances to be considered in making the determination of the worker's status.

As proposed, the six factors to be considered are as follows, but the Proposed Rule makes clear that the weight to be given to each factor is dependent upon the circumstances of each case:

- Opportunity for profit or loss depending on managerial skill: This factor requires a consideration of whether the worker determines or can meaningfully negotiate the charge or pay for the work provided; accepts or declines jobs or chooses the order and/or time in which the jobs are performed; markets or advertises the worker's business and seeks more work; and can hire others, purchase materials or equipment, and/or rent space. If the worker has no opportunity for profit or loss, the indication is that this person is an employee. The Proposed Rule states that a decision by the worker to simply work more hours or take on more jobs does not reflect the exercise of managerial skill

indicating independent contractor status.

- Investments by the worker and the employer: This factor considers whether any investments by a worker are capital or entrepreneurial in nature. These are investments that "generally support an independent business and serve a business-like function, such as increasing the worker's ability to do different types of or more work, reducing costs, or extending market reach." This factor is probably the most vague or enigmatic of the factors, and the preamble to the Proposed Rule provides no additional guidance other than to suggest that investments in the worker's business that would enable the worker to do more, broader, and different work from what the worker is doing for the employer and would be viewed to support independent contractor status.

- Degree of permanence of the work relationship: When the work relationship is indefinite or continuous, it is more likely to be deemed an employment relationship. When the work relationship is definite in duration, non-exclusive, project-based, or sporadic, the relationship is more likely to be deemed an employment relationship. However, the Proposed Rule offers numerous caveats that qualify this factor somewhat, including the statement that, "Where a lack of permanence is due to operational characteristics that are unique or intrinsic to particular businesses or industries and the workers they employ, rather than the workers' own independent business initiative, this factor is not indicative of independent contractor status." Although this factor is somewhat difficult to interpret, it appears that the DOL is suggesting that if the worker is driving the sporadic nature of the work as a result of being in business for themself and serving other entities, this factor will lean toward a finding of independent contractor status. Where the employer utilizes the worker sporadically simply because of the nature of the business (for example, if the employer utilizes non-employed nursing home assistants on a PRN basis due to absenteeism among its employed assistants), this factor will not support a determination that the workers are independent contractors.

- Nature and degree of control: This factor focuses on how much the employer controls the performance of the work and the economic aspects of the relationship, which has long been a factor considered by courts and the DOL and has often been viewed as the most important factor when determining independent contractor status. The factors that the Proposed Rule suggests are relevant to this analysis include whether the employer sets the worker's schedule, supervises the performance of the work, limits the worker's ability to work for other companies, "uses technological means of supervision (such as by means of a device or electronically)," has the right or ability to supervise or discipline workers (whether or not that right is actually exercised), or places such demands on workers' time that do not allow them to work for others or work when they choose (such as by scheduling the worker to perform services throughout a regular workday so the worker has no time to serve other clients/customers). The employer's control over prices or rates for services is also considered, if the worker has little to no negotiating power over the fees charge for their services, this factor weighs toward independent contractor status. Importantly, with this factor, the DOL states that "[c]ontrol implemented by the employer for purposes of complying with legal obligations, safety standards, or contractual or customer service standards" weighs in favor of employee status. The more control exerted by the employer over the worker and how the worker carries out the work, the more indication of employment status.

- The extent to which the work performed is an integral part of the employer's business: Whether the function the worker performs is an integral part is determined by examining whether the worker's work is critical, necessary, or central to the employer's principal business. This is a significant factor in the aforementioned ABC test, and is probably the clearest of the factors articulated in the Proposed Rule. In short, the "integral to the employer's business" factor means the worker is doing the key work of the business. If the business makes widgets, and the worker is working on the widget assembly line,

this factor would weigh toward a finding that the worker is an employee. If the business makes widgets and the worker provides high-level market analysis to determine emerging trends and revenue projections, the worker is less likely to be deemed an employee.

- Skill and initiative: This factor indicates employee status where the worker does not use specialized skills in performing the work or where the worker is dependent on training from the employer to perform the work. Where the worker brings specialized skills to the work relationship, the worker is more likely to be deemed an independent contractor.

The Proposed Rule makes clear that this list of factors is non-exhaustive; additional factors may be considered "if the factors in some way indicate whether the worker is in business for themself, as opposed to being economically dependent on the employer for work." Again, this provides a great deal more flexibility for employers to identify special and unique circumstances that warrant a finding of independent contractor status in a given worker/employer relationship.

From the standpoint of companies that need additional flexibility in fulfilling limited-duration functions that require specialized skill sets that their general workers do not have, this Proposed Rule appears to be business-friendly. The clear rejection of the ABC test in favor of a multifactor test that allows a great deal of flexibility and different weights means employers may have a good chance of demonstrating why, in a given situation, a worker engaged as an independent contractor is appropriately classified. Of course, the flexibility that is inherent in this "totality of the circumstances" test also means that employers may largely find themselves guessing about whether they have classified a worker correctly and whether a court or the DOL would agree with their analysis. In general, we consider this Proposed Rule to be a win.

Employers have 45 days after the published date to submit comments on the Proposed Rule. We will keep you updated about any developments on this issue.

If you have any questions about this topic, please contact Martha Boyd, Zachary Busey, or a member of Baker Donelson's Labor and Employment Group.