LABOR AND EMPLOYMENT ALERT | JANUARY 2021

U.S. DOL Publishes Final Rule Redefining Independent Contractor Standards Under FLSA

By M. Christine Carty

As anticipated, the Trump Administration Department of Labor ("DOL") published on January 6, 2021 final regulations redefining and simplifying the independent contractor standards under the Fair Labor Standards Act ("FLSA"). The new regulations are significant because the FLSA's minimum wage, overtime and record-keeping requirements do not apply to independent contractors.

Although the new regulations are slated to become effective on March 8, 2021, they face a cloudy future under the incoming Biden Administration. On December 30, 2020, Biden's press secretary, Jen Psaki, issued a statement criticizing the then-proposed DOL regulations, among others, as "midnight" rules that Biden intended to "halt or delay" immediately following the Inauguration.

KEY DETAILS

The new DOL regulations reaffirm that the "economic reality" test, not the common law agency test, determines whether a worker is an employee or independent contractor. According to the new regulations, the central determination in such an analysis is whether the worker is in business for himself or herself or dependent upon another person or entity for the work.

However, the new regulations reframe the independent contractor analysis by elevating two of the five familiar criteria to primary status and relegating the remaining three to a secondary, tie-breaker role. The new regulations may be found at Part 795 of the Code of Federal Regulations, 29 C.F.R. §§795.100, 105(a)-(d), 110 and 115.

The **two primary ("core") criteria** to determine a worker's status as an employee or independent contractor are (1) the nature and degree of the worker's control over the work and (2) the opportunity for profit or loss from personal "initiative" or investment by the worker.

The **three secondary factors** under the new regulations are (1) the specialized skill required to perform the services or job functions and whether the worker is dependent upon the business to provide the training for the skills, (2) the permanence or open-ended nature of the working relationship with the business, and (3) whether the services or job functions are part of an "integrated unit" of the employer.

The DOL regulations state that if the two "core" criteria – control and profit and loss – point to one status or the other, then there is a "substantial likelihood" that the classification indicated is correct and "highly unlikely" that the other three criteria, alone or together, will alter the outcome. The DOL commentary accompanying the proposed regulations make clear that the secondary criteria will be relevant ("probative") when there is a split decision; that is, the analysis of control and profit and loss is split between employee and independent contractor status.

For the first time, the regulations prescribe that a worker's personal "initiative" – identified to include managerial skill and business acumen – will be considered in weighing the ability of a worker to control profit and loss, in addition to the amount of capital investment by the worker. This definitional expansion is likely to benefit the gig economy and start-up businesses, including ride-sharing companies and online retail companies, where workers do not need a large

capital outlay for equipment, but depend upon their own business ingenuity, time management and identification of niche markets for their products or services.

ADDITIONAL CHANGES

Other changes and clarifications in the new regulations are:

- The actual practice and relationship between the worker and the business will be considered in determining proper classification, rather than theoretical possibilities or contractual rights.
- An exclusive relationship between the worker and the company or post-relationship restrictions strongly indicate control by the putative employer over workers, thus pointing the control factor toward employed status, regardless of the amount of day-to-day freedom to determine schedule and the order of performing the services.
- When examining the permanence of the relationship, only the duration and continuity of the relationship are to be considered. Exclusivity of the relationship is considered as part of the control analysis.
- In determining if the worker is part of an "integrated unit," the question to be answered is whether "the work is part of an integrated unit of production," not whether the work is central to the business of the company. The question is whether the worker is dependent upon the company's overall production process to perform his or her duties.

Notably for businesses, the DOL indicated in its explanations of the proposed regulations that economists did not expect reclassifications of workers, but rather that the new regulations would impact the classifications of new hires and workers in new businesses as independent contractors or employees.

ANALYSIS

Based on a strong statement made by the incoming Biden Administration, Biden may issue a memorandum on January 20 shortly after the Inauguration to prevent the DOL's FLSA rules and other regulations from becoming effective. According to the statement, "The Biden-Harris White House will issue a memo to take effect [on the] afternoon Eastern Time on January 20 that will halt or delay midnight regulations." Referring specifically to the new FLSA regulations of the DOL, the statement said: "[i]f it takes effect, that rule will make it easier to misclassify employees as independent contractors, costing workers more than $3.7 billion annually."

Biden's options may include: staying the effective date of the regulations; re-opening the rulemaking process and requesting additional comments from the public; or allowing the new regulations to become effective, but not defending the regulations if challenged in a litigation.

Businesses should continue to monitor closely whether the new standards will become effective and, in the meantime, consider whether the new regulations will require a change in classification of any groups of workers. The regulatory attention devoted to the classification criteria indicates the continuing importance of employer decisions affecting the classification of workers as employees or independent contractors. ◆

For more information about Schnader's Labor and Employment Practices Group, or to speak with a member of the firm, please contact:

M. Christine Carty
Partner
212-973-8012
ccarty@schnader.com

Jo Bennett
Co-Chair, Labor and Employment Practices Group
215-751-2134

jbennett@schnader.com

Michael J. Wietrzychowski
Co-Chair, Labor and Employment Practices Group
856-482-5723
mwietrzychowski@schnader.com

* *See: www.schnader.com/jakarta*