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Department of Labor Issues Final Independent Contractor Rule

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On January 10, 2024, the Department of Labor Wage and Hour Division published its Final Rule for determining whether an individual is an employee or an independent contractor under the Fair Labor Standards Act. This Final Rule officially rescinds the 2021 Rule issued under the previous administration. The 2021 Rule listed multiple economic factors to be considered but placed greater weight on two factors: the nature and degree of control over the work and the workers' opportunity for profit or loss.

The Final Rule, which is effective March 11, 2024, cautions employers that, although independent contractors are not covered by the FLSA, simply labeling workers as "independent contractors" does not create an independent contractor relationship. Instead, the Final Rule returns to the pre-2021 "economic reality test" emphasizing six factors to determine whether "the worker is economically dependent on the employer for work or is in business for themself." The six factors are:

- 1) *Opportunity for profit or loss depending on managerial skill.* This factor is designed to determine whether economic success or failure can be affected by the individual: by negotiating the charge or pay for the work provided; by deciding whether to accept or decline jobs; by engaging in marketing, or advertising to expand or secure more work; and by hiring others, purchasing materials and equipment, or renting space.
- 2) *Investments by the worker and the employer.* This factor examines whether the individual makes any capital investments into the business. For example, purchasing tools does not constitute investment in capital. Rather an investment that is "entrepreneurial in nature" refers to those that increase an individual's ability to do more work or different types of work, reducing costs, or expanding markets.
- 3) *Degree of permanence of the work relationship.* A relationship that is ongoing for an indefinite period would tend to demonstrate an employment relationship. On the other hand, project based or sporadic work that allows the individual to provide services to others would tend to support an independent contractor relationship.
- 4) *Nature and degree of control.* If the employer sets a schedule, supervises the work, or limits the individual's ability to work for others, this factor would support an employment relationship. The more control the employer has, the more likely an employer-employee relationship will be found.
- 5) *Extent to which the work performed is an integral part of the employer's business.* This factor is focused on the function, rather than the individual itself. If the employer's business is the same as the function being performed by the worker, then an employment relationship would likely be found.
- 6) *Skill and initiative.* The Department of Labor looks to whether the individual has a specialized skill or whether the individual is dependent on training provided by the employer. The more individualized the skill, the more likely an independent contractor relationship is supported.

The Final Rule will mean a change in status for many workers from "independent contractor" to "employee". Unfortunately, employers should be prepared for increased misclassification lawsuits. In light of the new rule and the significant risks of misclassification, employers should carefully scrutinize independent contractor relationships and related written agreements.

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