

US DOL's Independent Contractor Rule: What the Rule Means and How It Will Impact Workers

On October 11, the U.S. Department of Labor announced that it is proposing a new rule to determine who is an employee and who is an independent contractor under the Fair Labor Standards Act, the law that sets a federal minimum wage (currently \$7.25 per hour) and requires overtime (time and a half of a worker's hourly wage for every hour over 40 worked per week). This fact sheet explains what the rule means and how it will impact workers.

Why Employee Versus Independent Contractor Matters

In a nutshell, an employee works for someone else, while an independent contractor runs their own business.

Employees have rights and protections that independent contractors do not, including the right to a minimum wage and overtime, the right to a discrimination-free and harassment-free workplace, the right to join a union and collectively bargain, and the right to a safe and healthy workplace. Employees are also eligible for benefits—like workers' compensation and unemployment insurance—that independent contractors are not. Independent contractors are responsible for their own tax contributions and have other responsibilities that go with running their own business.

The DOL's proposed rule lays out guidance for determining who is an employee under the Fair Labor Standards Act (and therefore entitled to federal minimum and overtime wages) and who is an independent contractor (and therefore not protected under the Act).

Summary of the DOL's Proposed Rule

The DOL's proposed rule would rescind and replace a problematic rule adopted by the Trump administration. It proposes an analysis aimed at answering the key question: is the worker in business for themselves, or do they depend on finding work in the business of others? The proposed rule signals a return to a longstanding approach known as the "economic reality test." The test weighs the following six factors *and* explains how each factor should be analyzed:

1) Opportunity for profit or loss depending on managerial skill. This factor considers whether the worker exercises managerial skill that impacts their opportunity for profit or loss. If yes, this factor would suggest the worker is running an independent business so would weigh in favor of independent contractor status. A worker exercises managerial skill that impacts their opportunity for profit or loss if they:

- meaningfully negotiate the charge or pay for their work;
- make decisions on investments in their business, including whether to pay for marketing, advertising, or other efforts to expand the business; whether to purchase material, equipment, or rental space; and whether to hire others; and
- accept or decline jobs and choose the order or time in which jobs are performed.
- NOTE: A worker's *decision to work more hours* (when paid hourly) or work more jobs (when paid a flat fee per job) where the employer controls assignment of hours or jobs is *not* a reflection of managerial skill.

2) Investments by the worker and the employer. This factor considers whether the worker is making investments that are capital or entrepreneurial in nature (meaning investments that would support a business), which would weigh in favor of independent contractor status. A worker's investment also should be analyzed relative to the alleged employer's investment; if the alleged employer is making substantially more business investments than the worker, that would indicate the worker is an employee.

- Capital/entrepreneurial investments include: a decision to rent office space, buy advertising services, or buy equipment that increases the ability to do different or more types of work or reduces their cost.
- Here's an example from the DOL's proposed rule. "A graphic designer occasionally completes design projects for a local design firm. The graphic designer purchases their own design software, computer, drafting tools, and rents an office in a shared workspace. The worker also spends money to market their services. These types of investments support an independent business and are capital in nature (*e.g.*, they allow the worker to do more work and extend their market reach). Thus, these facts indicate that the worker is in business for themselves and may be a freelance graphic designer (*i.e.*, an independent contractor), not an employee of the local design firm."
- *However*, costs borne by a worker to do their job for a particular employer, such as tools or equipment to perform specific jobs, are *not* capital or entrepreneurial.
- *Similarly*, a worker's use of their personal car (or a car that the worker leases) to perform the work is *not* a capital or entrepreneurial investment.

3) Degree of permanence of the work relationship. This factor considers whether a work relationship is indefinite in duration or continuous, which suggests employee status, or whether the relationship is definite in duration, non-exclusive, project-based, or sporadic, thus indicating independent contractor status.

- *However*, if a worker’s sporadic, non-permanent relationship with an employer is due to the nature of the job (such as seasonal or temporary work), rather than the worker’s independent business decision, this factor will weigh toward employee status.
- 4) **Nature and degree of control.** This factor considers the alleged employer’s control—including ability or power to control, even if not exercised—over how the worker performs the work and over economic aspects of the relationship. Unless a worker has a great deal of control over their work, they are likely an employee. Aspects of control include:
- whether the employer can supervise the work (including through surveillance technology);
 - whether the employer can control economic aspects of the work relationship, such as setting the worker’s rate or prices and marketing the services or goods provided by the worker;
 - whether the employer can set the worker’s schedule (though the proposed rule says that scheduling flexibility is *not* as relevant as ability to set rates/prices); and
 - whether the employer can limit the worker’s ability to work for others, including by placing demands on time that make it functionally impossible to work for others or work when they choose.
- 5) **Whether the work performed is an integral part of the employer’s business.** This factor considers whether the worker’s job is central and necessary to the potential employer’s business. If so, the factor weighs in favor of employee status.
- Examples: a janitor working for a janitorial business, a tomato picker working for a farm, and a food delivery worker working for an app-based delivery company are all doing the central work of the employer’s business, which weighs toward employee status.
 - However, a janitor providing cleaning services for an advertising firm or an accountant providing payroll services to a farm are not doing the central work of the business.
- 6) **Skill and initiative.** This factor considers whether the work requires special skills *and* whether those skills help the worker exercise business-like initiative.
- If the worker does not use specialized skills in performing the work or is dependent on training from the employer to perform the work, this would suggest the worker is an employee.
 - If the worker has specialized skills *but* does not use those skills to build an independent business, then this would suggest the worker is an employee.
 - Example from the DOL’s proposed rule: “A highly skilled welder provides welding services for a construction firm. The welder does not make any independent judgments at the job site beyond the decisions necessary to do the work assigned. The welder does not determine the sequence of work, order additional materials, think about bidding the next job, or use those skills to obtain additional jobs, and is told what work to perform and where

to do it. In this scenario, the welder, although highly skilled technically, is not using those skills in a manner that evidences business-like initiative. The skill and initiative factor indicates employee status.”

FAQs about the Proposed Rule

What does this rule do?

This proposed rule will guide the DOL in determining whether an employer has violated the FLSA and whether to bring an enforcement action. It will also educate the public, including businesses and workers, on when businesses must comply with the FLSA because their workers are employees (and not independent contractors running their own businesses).

Here’s an example. A janitorial franchisee believes he is misclassified as an independent contractor. The janitorial franchisor (the alleged employer) finds the clients, negotiates the most important terms of the cleaning services (including what the client pays and when the cleaning gets done), and assigns the franchisee to these clients. The franchisee realizes that, after accounting for all his business expenses, he earns about \$5 per hour – far less than the federal minimum wage. He files a complaint with the DOL alleging that the franchisor is violating the FLSA.

When the DOL investigates the franchisee’s complaint, it must make an initial determination of whether the franchisee is properly classified as an independent contractor or is really an employee of the franchisor. To make that determination, the DOL will assess the franchisee’s working conditions under the “economic reality” test laid out in the rule.

If the DOL determines that the franchisee is a legitimate independent business, then the FLSA does not apply, because independent contractors are not covered. If the DOL determines that the franchisee is an employee who has been misclassified as an independent contractor, then it must determine whether the franchisor violated the FLSA by failing to pay minimum wage or overtime. If it determines the franchisor violated the law, it can bring an enforcement action against the franchisor to recoup back wages for the worker and to impose penalties on the franchisor.

Is this proposed rule a positive development?

Yes. As discussed above, the proposed rule clarifies how to analyze the six factors in the “economic reality test” with an eye toward determining whether a worker is in business for themselves or working for someone else.

For example, in analyzing factor 1 (opportunity for profit or loss depending on managerial skill), ***the proposed rule clarifies that a worker’s ability to work longer or harder (working more hours or picking up more jobs) is not, by itself, a reflection of managerial skill, so does not suggest the worker is running an independent business.***

In analyzing factor 2 (capital investments by the worker and employer), ***the proposed rule states that a worker’s use of their personal vehicle (or leasing a personal vehicle when***

required by the employer) to perform the work is not the type of entrepreneurial or capital investment that would suggest independent contractor status.

In analyzing factor 3 (degree and extent of control), the rule clarifies that that all of ways that an employer can control a worker must be considered, including how an employer may use technology to surveil, assign, or discipline workers. Furthermore, while the proposed rule says that whether an employer sets a work's schedule is one aspect of control, it is a minor one compared to other types of control, like ability to set wages and prices, which are stronger indicators of whether someone is running their own business. ***This means that scheduling flexibility alone does not indicate that a worker is free from the employer's control and thus is an independent contractor.***

Why does this rule matter?

This proposed rule makes clear that most workers are employees under the FLSA. This means the proposed rule will likely increase the number of workers covered under federal minimum wage and overtime requirements.

This is a big deal. Studies have found that many workers currently classified as independent contractors make less than minimum wage. For example, a **recent survey** of app-based workers (who are classified as independent contractors) found that 14 percent make less than the federal minimum wage. Similarly, a **recent report** by PolicyLink and Rideshare Drivers United found that app-based drivers average about \$6.20 per hour in pay. If those workers are found to be improperly classified under the DOL rule, then the DOL can bring enforcement actions to award backpay to those workers both for unpaid minimum wages and overtime.

Which workers and industries will this rule impact?

This proposed rule does not target a particular industry or occupation. It targets an illegal employer practice (misclassification) when that practice results in workers earning less than the federal minimum wage or their overtime wage. However, because misclassification is especially prevalent in low-wage, labor-intensive occupations where people of color and immigrants are overrepresented, including janitorial services, trucking and delivery services, and homecare and other domestic work, the proposed rule may especially improve compliance with the FLSA for workers in these occupations. This means the rule could help combat misclassification and restore minimum wage and overtime protections for the workers who need these protections most.

I believe I am misclassified as an independent contractor. Does this proposed rule mean that my employer will reclassify me as an employee?

Possibly. As discussed above, this rule will guide the DOL in determining whether an employer has violated the FLSA and whether to bring an enforcement action. If this proposed rule becomes final, some employers may determine, after applying the six-factor "economic reality" test, that their workers are misclassified, and the employer will reclassify its workers as employees rather than risk an enforcement action by the DOL.

However, other employers may decide not to reclassify their workers, figuring that they will wait to see if the DOL brings enforcement action. ***Therefore, it is critical that workers file complaints with the DOL.*** And we (workers and worker advocates alike) must also demand that Congress increase the DOL's budget, so that the DOL has the resources to do robust and comprehensive enforcement that will make this rule meaningful for workers.

Does this rule impact state and local laws, like California's AB5 and Prop 22, or campaigns to broaden access to state employment protections?

This proposed rule *only* determines whether someone is an employee or an independent contractor under the federal Fair Labor Standards Act. It does *not* determine whether someone is an employee or an independent contractor under state and local laws that provide rights and protections for employees. Such state laws include state minimum wage laws (31 states have laws that set a higher minimum wage than the federal minimum wage), state paid leave laws (11 states establish a right to paid family or medical leave for employees), as well as state laws that provide benefits to employees, like unemployment insurance and workers' compensation. State legislatures, courts, and administrative agencies make these determinations.

However, the DOL's proposed rule *may* have persuasive power, meaning that state courts and state administrative agencies *could* look to the DOL's new rule for guidance in interpreting who is an employee and who is an independent contractor under state laws.

Do states still need to pass new laws to combat misclassification or is the DOL independent contractor rule enough?

While the DOL independent contractor rule is an important first step, ***it is critical that workers and their representatives continue to advocate for stronger laws to combat misclassification at the state and local levels too.*** Several of the most vital employment rights and protections exist at the state and local level, including state laws that set a minimum wage higher than the federal minimum wage of \$7.25 per hour, state laws that provide a right to paid family and medical leave for employees, and state laws that require employers to provide information on pay and deductions to combat wage theft and promote pay transparency. State laws also create vital benefits programs for employees, including workers' compensation, unemployment insurance, and disability insurance. Stronger state laws that combat misclassification will ensure that all people working for someone else can access these critical state employment rights, protections and benefits.

I believe I am misclassified as an independent contractor, and my hourly wage is about \$13 per hour after accounting for my expenses. My state has a \$15 minimum wage. Can I get the DOL to bring an enforcement action for violation of my state's minimum wage law?

No. The DOL enforces the federal Fair Labor Standards Act, which sets the federal minimum wage (\$7.25) and overtime requirements, which provides for time-and-a-half pay when a

covered worker works more than 40 hours per week. The DOL does not enforce state laws, such as state laws that set higher minimum wages. You should file a complaint with your state labor agency.

Does this rule determine whether someone is an employee or an independent contractor under other federal laws, like the National Labor Relations Act (which establishes the right to join a union and collectively bargain) or Title VII (which prohibits discrimination based on race, color, religion, gender and national origin)?

No. This rule *only* determines whether someone is an employee or an independent contractor under the Fair Labor Standards Act. It does *not* determine whether someone is considered an employee or an independent contractor under other federal laws.

However, the DOL's proposed rule may have persuasive power with the agencies (like the EEOC or the NLRB) interpreting the scope of federal laws like the NLRA and Title VII. In fact, the NLRB is in the process of revisiting its employee/independent contractor standard (meaning who is an employee under the NLRA and has a right to join a union and collectively bargain) and should be publishing a decision on that soon.

Why isn't the DOL using the ABC test to determine who is an employee and who is an independent contractor?

The ABC test, which is an employee/independent contractor test used in many states' laws, starts with a presumption that all workers are employees. The hiring entity (potential employer) can rebut this presumption only if it shows that each of the following three conditions are met: (a) that the worker is free from the control and direction of the hirer in connection with the performance of the work, both under the contract for the performance of the work and in fact; *and* (b) that the worker performs work that is outside the usual course of the hiring entity's business; *and* (c) that the worker is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed. The ABC test is arguably a clearer and simpler standard for determining who is an employee and who is an independent contractor than the six-factor economic reality test.

However, as the DOL explained in its proposed rule, it must follow Supreme Court precedent interpreting the FLSA. The Supreme Court has said that the economic reality test is the right standard for determining whether a worker is an employee or an independent contractor under the FLSA. The DOL believes that Congress would need to pass legislation amending the FLSA and stating that the ABC test is the applicable standard in order for it to apply it.

How can I get involved in the DOL rulemaking and make my voice heard?

The DOL is accepting written comments from the public on its proposed rule until **December 13**. You can submit your comment [here](#).

Comments generally say whether the commenter is in favor of or against the proposed rule, and often include recommended changes to the proposed rule. ***But comments can take any form and can focus on any aspect of the proposed rule.*** For example, they can include affected workers discussing the impact of misclassification on their economic security and livelihood, or explanations of the ways that corporations use algorithmic management and technology to surveil and control their independent contractors (factor 4) in ways that strongly suggest these workers are misclassified.

It is critical that the DOL hear from a diverse group of workers about the impact of the proposed rule. NELP encourages workers and worker member organizations to comment and make their voices heard. We are happy to strategize with you about your comment.