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U.S. Department of Labor Issues Final Rule on Independent Contractors

On January 10, the U.S. Department of Labor (DOL) issued its final rule on the definition of “independent contractors” under the Fair Labor Standards Act (FLSA). This rule rescinds the 2021 rule and claims to be more consistent with longstanding judicial precedent interpreting the FLSA. The final rule employs a flexible “totality-of-circumstances” test to assess economic reality, as used by many courts. The final rule is expected to take effect on March 11, 2024.

Why it matters

Under the FLSA, “employees” are protected by federal wage-and-hour laws regarding minimum wage, overtime, and recordkeeping. “Independent contractors” are not covered by the FLSA protections. If a worker is misclassified, businesses are subject to penalties under the FLSA.

The new rule

The DOL’s final rule is a return to a “totality-of-the-circumstances” analysis where no one factor is dispositive. This contrasts with the 2021 rule which placed greater emphasis on two “core factors”—control over the worker and the worker’s opportunity for profit or loss.

Under the new rule, the central inquiry is whether the individual is “economically dependent” on the potential employer. An “employee” is “economically dependent on an employer for work,” whereas an “independent contractor” is “in business for themselves.” To determine economic dependence, the rule outlines six factors which the DOL will consider:

1. Opportunity for Profit or Loss Depending on Managerial Skill
2. Investments by the Worker and the Potential Employer

3. Degree of Permanence of Work Relationship
4. Nature and Degree of Control
5. Extent to Which the Work Performed Is an Integral Part of the Potential Employer's Business
6. Skill and Initiative

However, these factors are non-exhaustive, and the DOL may consider additional factors if they reflect the worker's independence from the potential employer.

Differences from 2021 rule

By weighing all factors equally, the new rule applies more broadly than the 2021 rule, which the DOL claims limited consideration of relevant factors considered by courts ruling on the FLSA. The DOL states that the new rule will reduce misclassification and eliminate the confusion caused by the previous rule ignoring "decades of case law" that applied the totality-of-circumstances test.

Now, the "control" factor considers not only the potential employer's exercised control but also the potential employer's reserved control, even if not exercised. This contrasts with the 2021 rule which minimized the potential employer's reserved control. Facts relevant to control include: setting work schedules, supervision of work, and limitation of the worker's ability to work for others. Further, the new rule delves into the potential employer's actions regarding compliance with laws or regulations, and when those actions may be indicia of control.

In addition, the new rule focuses on whether the work performed is "an integral part of the potential employer's business," whereas the 2021 rule focused on whether an individual worker was an integral part of the business. This new language focuses on the function, rather than the individual. Work that is found to be "critical, necessary, or central" to the potential employer's principal business weighs in favor of the worker being an employee.

What this means to you

Businesses relying on independent contractors should closely examine the new rule. Some industry professionals worry that the final rule is ambiguous and difficult to interpret and will result in more confusion and unnecessary litigation over who qualifies as an independent contractor. Others, like the DOL and labor unions, assert that the new rule is in fact clearer and will avoid independent contractor misclassification, reduce wage theft, and prevent employers from undercutting their law-abiding competition.

Given the pattern of increased litigation following regulatory changes, businesses should evaluate their worker classifications, assess litigation risks, and make adjustments to stay compliant with the new rule.

Contact us

If you have any questions about worker classifications or potential adjustments, contact Julianne Story, Eric Locker, or your Husch Blackwell attorney.