

Department of Labor Issues New Guidance on Who is an Independent Contractor

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The Department of Labor is focused on eliminating what they believe to be an increasing number of employees who are misclassified by their employers as being independent contractors, and therefore ineligible for benefits, overtime pay, workers compensation and other perks of being an employee.

To that end, the DOL has just issued an “Administrator’s Interpretation” which substantially changes the test for whether a worker is an employee or an independent contractor.

The old test was essentially one of control. To what extent did the employer control the means and methods of the work? Did the employer set the work schedule, instruct the worker on how to do the work, provide the tools for doing the work, etc.

The new test is much different, and make no mistake it is designed to make it harder than ever to classify a worker as being an independent contractor.

The new test is called the “economic realities” test. The question now is whether the worker is economically dependent on the entity that is paying him or truly in business or himself or herself. A quick summary of the new factors in that test is as follows:

- 1. Is the work an integral part of the employer’s business?** If it is, the worker is less likely to be an independent contractor. The examples that they give are a construction company hiring a carpenter to frame houses. That is integral to the business of the construction company and the individual is likely an employee. But that same construction company that contracts with a software developer to develop software for use by the company is likely an independent contractor as that work is not integral to the employer’s business.
- 2. Does the worker’s managerial skill affect his or her opportunity for profit or loss?** This factor looks to whether the worker has an opportunity not just for profit, but for loss, both of which are hallmarks of someone in business for themselves. If the worker makes decisions such as who to hire, how much to pay them, what materials and equipment to purchase, whether and how to advertise, whether to rent space for the business, etc., he or she is making managerial decisions that could affect profit or loss (note, this factor is not working extra hours to make money, as the DOL believes that this is the same for employees as for independent contractors).
- 3. How does the worker’s relative investment compare to the employer’s investment?** This factor looks to whether the worker has made an investment (and thus has some risk of loss) that supports the business outside of any particular job. Investing in tools and equipment may not be enough, as employees often do that as well. It needs to be a significant business investment, which can include tools and equipment, but also such things as company vehicles, office space, storage space, etc.
- 4. Does the work require special skill and initiative?** This factor looks to the worker’s business skills, judgment and initiative, not his or her technical skills.
- 5. Is the relationship permanent or indefinite?** A permanent relationship, or one that is of indefinite duration, suggests that the worker is an employee. An independent contractor typically works a project for one employer, then another for

another employer, etc. Therefore, the longer the worker works just for one employer, the more likely he or she is to be an employee.

6. The nature and degree of the employer's control? The old control test is still around, but only as one of the many factors looked at. This factor looks at whether the worker actually exerts control over meaningful aspects of the work. The DOL is not impressed by independence in working hours, as they point out that this is becoming more common even for employees (especially those that work from home). Rather, it is control over schedules, dress, tasks carried out, and the like. The DOL warns that this factor is not very significant.

SUMMARY

It appears that these factors may be placed in the order of importance as the DOL sees them, so the first few factors are likely the most important. However, the DOL stresses that none of the above factors is 100% determinative. Therefore, an employer needs to be aware of all of them and should try to meet as many as possible in order to maintain an independent contractor relationship, keeping in mind that the intent of the DOL with this new guidance is to correct what they believe to be rampant misclassification of workers.

If you regularly use independent contractors, we urge you to contact me to more fully discuss the DOL guidance, which is much more extensive than the above summary, so that we can determine what strategy you should follow. The options would be to reclassify them as employees, make changes to your relationship to make sure they remain independent contractors, or, potentially, leave things as they are. Over the next year and a half, this is going to be a major emphasis for enforcement by the DOL.

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