Patterson Belknap

Employment Law Alert
March 19, 2024

Labor Department Issues New Independent Contractor Rule

On January 10, 2024, the Wage and Hour Division of the United States Department of Labor ("DOL") published a final rule (the "Final Rule"), which became effective on March 11, 2024, modifying the DOL's guidance on how to analyze who qualifies as an employee or an independent contractor under the Fair Labor Standards Act ("FLSA"). The Final Rule rescinds an earlier rule (the "2021 Rule") and, according to the DOL, replaces it with guidance that is more consistent with the text and purpose of the FLSA. In addition, the DOL expects the Final Rule to provide greater consistency for businesses.

As discussed in an earlier client alert, this is not the first time the DOL has modified its independent contractor guidance in recent years. Given this continuously evolving landscape, employers should promptly consider how the Final Rule may impact their worker classifications.

Overview of the Final Rule

The Economic Realities Test

Federal courts generally use a six-factor "economic realities" test to determine whether a worker qualifies as an employee or independent contractor under the FLSA. Those factors are:

1. **Does the worker's managerial skill affect his or her opportunity for profit or loss?** (If so, the worker is more likely an independent contractor.)

2. **How does the worker's investment compare to the employer's investment?** (A higher investment by the worker makes it more likely that he or she is an independent contractor.)

3. **Is the relationship between the worker and the employer permanent or indefinite?** (If the relationship is finite in duration, sporadic, or non-exclusive, the worker is more likely an independent contractor.)

4. **What is the nature and degree of the employer's control over the worker?** (The less control exercised by the employer, the more likely the worker is an independent contractor.)

5. **Is the work performed by the worker an integral part of the employer's business?** (The less integral the work is, the more likely that the worker is an independent contractor.)

6. **Does the work require special skill and initiative?** (If so, the worker is more likely an independent contractor.)

In evaluating the presence (or absence) of these factors, the Final Rule advises that the DOL will consider all six factors based on the totality of the circumstances. Thus, no one factor, or group of factors, has any predetermined weight. Further, the Final Rule underscores that the "ultimate inquiry" is whether, as a matter of economic reality, a worker is economically dependent on the employer for work (and is therefore an employee) or is in business for him or herself (and is therefore an independent contractor).

Noteworthy Changes from the 2021 Rule

The Final Rule includes several substantive changes from the 2021 Rule. First, the 2021 Rule instructed that the DOL would consider five, rather than six, factors in applying the economic realities test. In particular, factor 2 (investments by the worker and employer) was not considered an

independent factor. Consistent with the approach taken by many federal courts, the Final Rule departs from the 2021 Rule and considers investments made by the worker and the employer as a standalone inquiry.

In addition, the 2021 Rule designated two "core factors" (opportunity for profit or loss and the employer's nature and degree of control) as carrying more weight in the analysis than the others. In contrast, the Final Rule places no particular importance on any one factor and instead encourages a case-by-case factual assessment.

Finally, the Final Rule provides additional context and analysis to several factors, including a discussion of exclusivity in the context of the permanency factor, initiative in the context of the skill factor, and a discussion of scheduling and supervision in the context of the control factor.

Key Takeaways for Employers

Now that the Final Rule is in effect, employers should review any relevant contracts, policies, and/or procedures to ensure that their workers are properly classified under applicable guidelines and regulations. In implementing any revisions, employers should be mindful that the Final Rule applies only to the DOL's interpretation of the FLSA, and does not otherwise modify obligations imposed by federal, state, or local law. Employers should therefore consider New York State guidance and publications on which workers qualify as independent contractors before implementing any changes.

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