New Department of Labor Rule Restores Multifactor Analysis for Classifying Workers as Employees or Independent Contractors

Article By:
Jessica L. Westerman

Effective March 11, 2024, a new administrative rule will modify how the Department of Labor (DOL or Department) classifies workers as either employees or independent contractors under the Fair Labor Standards Act (FLSA). The 2024 rule will rescind the 2021 rule currently in place, which focused the Department’s classification analysis on two “core factors,” and restores the multifactor analysis that previously had been in use by courts for decades.

Given the procedural uncertainty surrounding the 2021 rule, its impact on FLSA jurisprudence has been minimal-to-nonexistent. In this sense, the 2024 rule merely codifies an analysis that federal courts never really stopped using, in the first place. But it also sends an important signal to employers operating in the modern economy: even if workers have significant autonomy over their day-to-day work lives, they should be classified as employees if, as a matter of economic reality, they are dependent on their employer’s business for work.

**Background on the FLSA and Pre-2021 Classification Analysis**

Under the FLSA, employers generally must pay employees at least the federal minimum wage for all hours worked and at least one and one-half times the employee’s regular rate of pay for every hour worked over 40 in a single workweek. The FLSA does not, however, extend these and other workplace protections to workers who are classified as independent contractors. Employees who are misclassified as independent contractors therefore may incur substantial losses in unpaid overtime and other lost wages as a result of their status.

Prior to 2021, federal courts applied flexible, multifactor tests rooted in Supreme Court precedent to determine whether workers should be classified as employees, and thus covered by the FLSA, or independent contractors, and thus excluded from FLSA coverage. The “ultimate inquiry” was whether, as a matter of economic reality, the worker was economically dependent on the business entity for work (employee) or was in business for herself (independent contractor).

Though the specific factors varied somewhat by circuit, the tests generally took into consideration (1) workers’ opportunity for profit or loss; (2) the amount of investment in the business by the worker; (3) the permanency of the working relationship; (4) the business’s control over the worker; (5) whether...
the work constituted an “integral part” of the business; and (6) the skill and initiative required to do
the worker’s job. Courts tended not to assign predetermined weight to any factor or factors and
engaged in a “totality-of-the-circumstances” analysis.

Prior to 2021, DOL had issued only informal guidance on classifying workers as employees or
independent contractors and other than some industry-specific guidance—for example, for
sharecroppers and tenant farmers and certain workers in the forestry and logging industries—had not
engaged in formal rulemaking on this topic. Rather, the Department allowed federal courts to develop
and hone their own classification analyses on a case-by-case basis.

**The 2021 Rule**

On January 7, 2021, DOL promulgated a first-of-its-kind rule identifying a total of five factors, but
prioritizing only two “core factors,” for federal courts to consider in conducting the classification
analysis. DOL articulated the two “core factors” as (1) the nature and degree of the worker’s control
over the work and (2) the worker’s opportunity for profit or loss based on initiative, investment, or
both. It articulated the three remaining factors as (3) the amount of skill required for the work; (4) the
degree of permanence of the working relationship between the individual and the business; and (5)
whether the work is part of an “integrated unit of production.” If the two “core factors” weighed in
favor of the same classification, it likely was the correct classification, and the Department deemed it
“highly unlikely” the three non-core factors could outweigh the combined probative value of the other
two.

By elevating the two “core factors” above the other factors traditionally considered by federal courts,
the 2021 rule focused almost exclusively on workers’ control over when and on what projects they
worked and their ability to earn more money based on how efficiently or for how long they worked.
This approach ignored the reality that for many workers, their work is completely dependent on their
employer’s business—and vice versa—even though they may have significant autonomy over their day-
to-day work lives.

The Department’s articulation of some of the non-core factors also departed from longstanding court
precedent and rendered them less, not more, compatible with the modern economy. For example,
the 2021 rule considered only whether a worker’s job was part of an “integrated unit of production,”
akin to a job on an assembly line, rather than its importance or centrality to the business, overall. This
change risked misclassifying employees who performed work that was essential to but “segregable
from” an employer’s process of production or provision of services, even though modern industry is
much more sprawling than the traditional assembly line. The 2021 rule also combined the distinct
“investment in the business” factor with consideration of a worker’s potential for profit and loss,
which improperly shifted the focus of that factor from worker inputs to worker outcomes. This change
likewise risked misclassifying employees who earned more profits because of greater “investment” in
their employers’ businesses, even though the costs they bore might have been non-capital
in nature, e.g., an existing personal vehicle, or imposed unilaterally by the employers.

Shortly after the change in administration that took place on January 20, 2021, the Department took
steps to delay and ultimately withdraw the 2021 rule based on these and other concerns about its
potential to misclassify employees as independent contractors. But legal challenges to the
administrative process led a Texas district court to vacate the Department’s delay and withdrawal
actions, ostensibly leaving the 2021 rule in effect. Though the Department appealed the district
court’s order, the Fifth Circuit stayed the action pending promulgation of the new rule. In the interim,
the uncertain legal status of the 2021 rule and impending new rule meant that few courts, if any,
incorporated the “core factor” analysis into their jurisprudence.[1]

The 2024 Rule

After unsuccessful efforts to delay and withdraw the 2021 rule, the Department opted to rescind and replace it altogether with the new final rule it announced on January 10, 2024. The 2024 rule, effective March 11, 2024, identifies six equally-weighted factors for courts to consider in classifying workers as independent contractors or employees: (1) opportunity for profit or loss depending on managerial skill; (2) investments by the worker and the potential employer; (3) degree of permanence of the 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; and (6) skill and initiative. Each single factor should be considered “in view of the economic reality of the whole activity” and additional factors “may be relevant” to the analysis.

Notably, the 2024 rule reverts to the “integral to the business” formulation of that factor; treats “investment in the business” as a distinct factor; differentiates between capital and non-capital investments by workers; and takes into consideration whether a particular cost was incurred based on entrepreneurial initiative or was imposed unilaterally by the employer. In these ways, the 2024 rule is much more compatible with the growing and increasingly diffuse economy than was the 2021 rule.

Ongoing and prospective legal challenges to the 2024 rule, plus the looming possibility that the Supreme Court will overturn or modify *Chevron v. Natural Resources Defense Council*—the 1984 decision applying deference to a federal agency’s interpretation of the statutes it administers—mean the 2024 rule may have a limited impact on FLSA jurisprudence. But it nevertheless conveys the Department’s position that employers should err on the side of classifying workers as employees, not independent contractors, and therefore subject to FLSA protections.

Given this changing landscape, employers may struggle to classify workers who were considered independent contractors under the 2021 rule but will be considered employees under the 2024 rule. If your employer has misclassified you as an independent contractor instead of an employee, you may be entitled to benefits and protections under the FLSA or state equivalents, like time-and-a-half pay for overtime work, that you are not currently receiving. If you believe you have been misclassified, consider contacting an attorney to discuss your legal options.


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