


# Think your worker is an independent contractor? Think again.




Patricia W. Goodson

August 3, 2015

Subscribe to News and Insights

 Via RSS

 Via Email



As part of its ongoing Misclassification Initiative, on July 15, 2015, the United States Department of Labor (“DOL”) issued a memorandum clarifying the line between independent contractors and employees: the “suffer or permit standard.” No longer will the common law control test hold. Now, the DOL directs employers to look to the “economic realities” of the worker’s situation: whether the worker economically depends on the employer. If the worker economically depends on the employer, under this guidance, the worker is an employee. According to the DOL, “applying the economic realities test in view of the broad definition of ‘employ’ under the Act, most workers are employees under the FLSA.”

The DOL considers classification of workers critical because an employee is covered by workers’ compensation insurance, entitled to minimum wage and overtime compensation, and unemployment benefits, while an independent contractor is not. An employer’s own classification of a worker’s status is irrelevant. Review these “economic realities” factors and incorporate them into your classification process—failing to do so welcomes a DOL investigation and expensive penalties. The DOL has entered into memoranda of understanding with many states and the IRS as part of the Initiative and is actively pursuing complaints.

## Key Factors to Consider

The DOL guidance lists six factors to consider when deciding whether a worker is **economically dependent**. No single factor is dispositive, and the application of these factors is guided by the principle that the FLSA should be construed to provide broad coverage to workers.

1. **The extent to which the work performed is an integral part of the employer's business.**

Work that is integral to the employer's business indicates an employer-employee relationship. Whether workers are integral to a business does not depend on whether they are easily replaceable. For example, a worker making calls at a call center may be one of hundreds but his work is still integral to the business purpose of the call center. Furthermore, work can be integral to the employer's business no matter where the worker is when performing it: at home, on the employer's premises, or on a customer's premises.

2. **The worker's opportunity for the worker's own profit or loss depending the worker's managerial skill.**

The more managerial responsibility affecting profits and losses a worker has, the more likely she is an independent contractor. Decisions such as whether to hire others, purchase materials and equipment, advertise, rent space, and manage time tables reflect profit- and loss-making managerial skills and allow an independent contractor to be truly that: independent. She can engage her managerial skills (or not) to increase her profit...and if she does not, she is responsible for her loss. In contrast, an employee does not typically have the ability to make decisions affecting her ability to make more money except to decide to work more hours. Working longer hours to increase earnings does not indicate managerial responsibility. Moreover, the employee does not face the prospect of a loss the way an independent contractor would.

3. **The extent of the relative investments of the employer and the worker.**

An independent contractor makes investments that support the worker's business beyond any one job, and employers must compare that investment with their own. The larger the relative worker-funded investment compares with the employer's investment, the more likely she operates as an independent contractor. Employers must consider their own investments as a whole—not only in the particular job performed by the worker. If the worker's investment is relatively minor, that suggests the worker and the employer are not on similar footing, and that the worker may be economically dependent on the employer.

4. **Whether the work performed requires special skills and initiative.**

A worker's business skills, judgment, and initiative, not his or her technical skills, are determinative in assessing whether the worker is economically independent. For example, cable installers, carpenters, and electricians all have technical skills. For those skills to be indicative of independent contractor status, they should be used in some independent way, such as demonstrating business-like initiative by determining the sequence of the work, ordering additional materials, or working on bidding another job. The worker should be operating as an independent business, as opposed to being told what work to perform where, which makes the worker economically depending on the employer, and, therefore, an employee.

5. **The permanency of the relationship.**

Transient relationships indicate the worker is an independent contractor and permanent or indefinite engagements suggest an employer-employee relationship. But the employer must look to whether that lack of permanency is due to the operational characteristics intrinsic to the industry or the worker's own business initiative. If the lack of permanency is due to the characteristics of the industry (for example, an industry that regularly relies on part-time workers or staffing agencies), then the worker still may be an employee. The DOL reasons that a true independent contractor would not want a permanent or indefinite relationship because of the dependence on one source of income.

6. **The degree of control exercised or retained by the employer.**

The worker must exercise control over meaningful aspects of the work to be seen as a truly independent businessperson and an independent contractor. The reason for an employer's control over a worker is irrelevant—it is the nature and degree of the employer's control, not the reason for it. If an employer must maintain significant control over a worker as a business need, it may need to hire employees instead of independent contractors.

## What Employers Must Do Now

- 1) **Assess your worker relationship classification.** The DOL does not care whether you label your workers as independent –if the economic realities of the workers’ situations deem them employees, they are. Correct classification now may save litigation costs and penalties later.
- 2) **Do not rely on old determinations that a worker is an independent contractor** According to the DOL, even some courts have misclassified workers as independent contractors. Do not rely on determinations that may have followed the common law control test or an antiquated version of the economic realities test.
- 3) **Seek advice.** This DOL memorandum introduced concepts many employers never have previously considered. Talk to an experienced employment lawyer if you have any questions about distinguishing any of these factors or for advice regarding your current classifications.