

## **U.S. Department of Labor Independent Contractor Final Rulemaking**

On Jan. 10, 2024, the U.S. Department of Labor (DOL) Wage and Hour Division published its final Independent Contractor (IC) rule, *Employee or Independent Contractor Classification Under the Fair Labor Standards Act* (89 Fed. Reg. 1638). The rule sets the standard, or test, used by courts in determining whether a worker is properly classified as an IC under the Fair Labor Standards Act (FLSA). According to the DOL, the rule “restores the multifactor analysis used by courts for decades, ensuring that all relevant factors are analyzed to determine whether a worker is an employee or an independent contractor.”<sup>1</sup>

To clarify the purpose of the rule, the DOL provides, “As used in this rule, the term ‘independent contractor’ refers to workers who, as a matter of economic reality, are not economically dependent on an employer for work and are in business for themselves. Such workers play an important role in the economy and are commonly referred to by different names, including independent contractor, self-employed, and freelancer. This rule is not intended to disrupt the businesses of independent contractors who are, as a matter of economic reality, in business for themselves.”<sup>2</sup> In short, “Instead of using the ‘core factors’ set forth in the 2021 IC Rule, this final rule returns to a totality-of-the-circumstances analysis of the economic reality test in which the factors do not have a predetermined weight and are considered in view of the economic reality of the whole activity.”<sup>3</sup>

The rule rescinds and replaces a Trump-era rule (2021 IC Rule) “which used a five-factor economic reality test comprised of two more probative ‘core factors’ and three less probative ‘non-core’ factors.”

The rule adopts the following six-factor totality-of-the-circumstances analysis<sup>4</sup>:

- (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

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<sup>1</sup> *US Department of Labor Announces Final Rule on Classifying Workers as Employees or Independent Contractors under the Fair Labor Standards Act*; USDOL News Release; (Jan. 9, 2024); Access at: <https://www.dol.gov/newsroom/releases/whd/whd20240109-1>

<sup>2</sup> *Employee or Independent Contractor Classification Under the Fair Labor Standards Act*, 87 Fed. Reg. 62,218 (Oct. 13, 2022). Access at: <https://www.federalregister.gov/documents/2022/10/13/2022-21454/employee-or-independent-contractor-classification-under-the-fair-labor-standards-act>

<sup>3</sup> *Id.*

<sup>4</sup> *U.S. Department of Labor Promulgates Final Independent Contractor Rule Under the Fair Labor Standards Act*, Paul, Weiss, Rifkind, Wharton & Garrison LLP (Jan. 19, 2024); Access at: <https://www.paulweiss.com/practices/litigation/employment-workplace-investigations-trade-secrets/publications/us-department-of-labor-promulgates-final-independent-contractor-rule-under-the-fair-labor-standards-act?id=49933>.

## (6) skill and initiative<sup>5</sup>

As provided by employment law firm Hunton Andrews Kurth, “In terms of legal compliance, the rule clarifies that the control necessary to comply with specific legal requirements does not automatically classify a worker as an employee. However, additional control exercised for convenience beyond legal necessities may influence the overall analysis. Second, the rule shifts from a dollar-for-dollar comparison in the assessment of relative investments. Instead, it focuses on whether the worker is making ‘similar types of investments,’ indicating a move towards independent operation. Third, in evaluating tools and equipment, the final rule considers costs unilaterally imposed by the potential employer, distinguishing them from those initiated by the worker, in determining independence. Fourth, regarding profit or loss, the rule specifies that the ability to earn more by working more is not entrepreneurial when paid a fixed rate per hour or job, but other payment methods may suggest independence. Lastly, the rule emphasizes that specialized skill alone does not automatically confer independent contractor status; the key factor is whether the worker uses specialized skill in connection with business-like initiative. These nuanced adjustments aim to provide clearer guidance for employers and workers navigating the intricate landscape of independent contractor classification.”<sup>6</sup>

The rule is set to go into effect on March 11, 2024, but has already been met with multiple legal challenges in federal court from freelancer and business groups. The U.S. Chamber of Commerce and various states attorney general have also signaled they may file legal challenges. We will continue to keep AAPL members updated should a federal court stay (delay) the rule pending litigation.

For background, in the final days of the Trump administration, the DOL finalized a new regulation

## Former vs. New Rule Comparison

### Former 2021 DOL Rule

On Jan. 6, 2021, the DOL published a five-factor “economic realities” test during the final days of the Trump administration, used to determine whether a worker is in business for themselves (an independent contractor) or economically dependent on an employer (an employee).

The five factors are:

- (1) The nature and degree of the worker’s control over the work;
- (2) The worker’s opportunity for profit or loss;
- (3) The amount of skill required for the work;
- (4) The degree of permanence in the working relationship; and
- (5) Whether the work is part of an integrated unit of production

The 2021 rule relied heavily on the first two factors, which were designated as “core factors” to be accorded more probative weight than the others and were considered more favorable to a recognition of IC status. If the first two factors weighed in favor of IC classification, it was “highly unlikely” that the three remaining factors would outweigh the first two.

### New 2024 DOL Rule

On Jan. 10, 2024, the Biden administration released a new IC rule that restores a multifactor analysis test in effect during the Obama administration that weighs all relevant factors under a “totality of the circumstances” economic reality test in which no one factor weighs more heavily than the others.

The six factors are:

- (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

The new rule affirms the ultimate inquiry of economic dependence and notes that worker would not be considered an IC if the worker is economically dependent on an employer for work. However, the DOL provides that other factors in addition to the above six may be relevant to determine if a worker is in business for themselves.

SOURCE: U.S. Department of Labor 2021; 2024

<sup>5</sup> *Frequently Asked Questions - Final Rule: Employee or Independent Contractor Classification Under the FLSA*; USDOL; Access at: <https://www.dol.gov/agencies/whd/flsa/misclassification/rulemaking/faqs#7>

<sup>6</sup> *DOL’s New Six-Factor “Economic Realities” Test: Navigating Changes in Independent Contractor Classification*; Hunton Andrew Kurth LLP (Jan. 22, 2024); Access at: <https://www.huntonlaborblog.com/2024/01/articles/agency-developments/dols-new-six-factor-economic-realities-test-navigating-changes-in-independent-contractor-classification/#page=1>

regarding the test used to determine IC status under the FLSA that was interpreted as providing a more flexible and permissive reading to support IC status under the FLSA rather than a determination that a worker was an employee in circumstances where disputes arose. Since early 2021, the Biden administration had sought to rescind that rule but faced various legal setbacks in federal court, leaving the Trump rulemaking in place until issuing a proposed rule in 2022 to amend the IC standard.

On Oct. 13, 2022, the DOL published a proposed rule, stating “that the misclassification of employees as independent contractors remains ‘one of most serious problems’ facing workers and businesses.”<sup>7</sup> According to the proposed rule, “the 2021 IC Rule narrowed the economic reality test by limiting the facts that may be considered as part of the test, such as consideration of whether the work performed by a worker is central to the employer’s business, which the DOL believed is relevant in determining the ultimate inquiry.” As such, the proposed rule “clarified that the ultimate inquiry is whether, as a matter of economic reality, the worker is either ‘economically dependent on the employer for work or in business for themselves.’ To answer this ultimate inquiry of economic dependence, the DOL set forth six non-exclusive factors to be evaluated under a totality of the circumstances framework.”<sup>8</sup>

At that time, AAPL provided members with an opportunity to submit public comments on the proposed DOL rule. We also provided members with an in-depth Fact Sheet which provided analysis and a side-by-side comparison of how the Biden administration rule compared to the rule under the Trump administration. The DOL reported receiving more than 54,000 public comments on the proposal and in the end issued a final rule that largely conformed to the proposed rule with slight modifications.

As noted above, the final rule adopts the “economic realities test that analyzes an employee’s classification through the totality of the circumstances of the worker-employer relationship.” The rule also “affirms the same ultimate inquiry of economic dependence and notes that a worker is not an independent contractor if the worker is economically dependent on an employer for work.” Importantly, unlike the proposed rule, the final rule provides that “factors in addition to the above six factors may be relevant if those factors indicate a worker is in business for themselves rather than being economically dependent on the potential employer for work, which according to the DOL, is the ‘ultimate inquiry’ for determining independent contractor status.”<sup>9</sup> This caveat has alleviated initial concerns that the rule could have nearly eliminated independent contractor classifications.

National corporate law firm Paul, Weiss, Rifkind, Wharton & Garrison LLP provides the following implications for employers/hiring companies:

- As the Final Rule only addresses classification of workers under the FLSA, employers are encouraged to take steps to maintain compliance with all other potentially relevant federal, state and local laws concerning classification of workers.
- Employers should consider reviewing and updating independent contractor agreements with an eye toward compliance with the Final Rule, recognizing that the ultimate inquiry is whether, as a matter of economic reality, the worker is either “economically dependent on the employer for work or in business for themselves.”

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<sup>7</sup> *Employee or Independent Contractor Classification Under the Fair Labor Standards Act*, 87 Fed. Reg. 62,218 (Oct. 13, 2022). Access at: <https://www.federalregister.gov/documents/2022/10/13/2022-21454/employee-or-independent-contractor-classification-under-the-fair-labor-standards-act>

<sup>8</sup> *Id.* at 1.

<sup>9</sup> *Id.*

- Employers should consider evaluating the economic reality/actual practice surrounding their independent contractor and employee relationships against the Final Rule test to ensure proper classifications under the FLSA.
- Given that the lawsuit surrounding the DOL’s delay and withdrawal of the 2021 IC Rule is still pending, employers may consider monitoring the Final Rule for any further developments, including any potential legal challenges against the Final Rule.<sup>10</sup>

## Additional Resources

Following is a list of additional resources for a deeper dive into the rulemaking, how it would be applied when a dispute arises, and the implications for businesses and workers:

- *Reality Check: U.S. Department of Labor Finalizes Worker Classification Rule* (Brownstein Hyatt Farber Schreck, LLP; Jan. 10, 2024):  
<https://www.bhfs.com/insights/alerts-articles/2024/reality-check-u-s-department-of-labor-finalizes-worker-classification-rule>
- *DOL Releases New Independent Contractor Rule* (Proskauer Rose LLP; Jan. 9, 2024):  
<https://www.lawandtheworkplace.com/2024/01/dol-releases-new-independent-contractor-rule/#page=1>
- *Employers Face Greater Misclassification Risk Under Resurrected Federal Independent Contractor Rule, Opening Door to Substantial Liability* (Pillsbury Winthrop Shaw Pittman LLP; Jan. 17, 2024):  
<https://www.pillsburylaw.com/en/news-and-insights/dol-fair-labor-standards-act-contractors.html>
- *DOL Issues Independent Contractor Final Rule* (SHRM; Jan. 9, 2024):  
<https://www.shrm.org/topics-tools/employment-law-compliance/dol-issues-independent-contractor-final-rule>
- *U.S. Department of Labor Finalizes Independent Contractor Regulation* (Littler Mendelson P.C.; Jan. 9, 2024):  
<https://www.littler.com/publication-press/publication/us-department-labor-finalizes-independent-contractor-regulation>

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<sup>10</sup> *Id.*