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# Understanding The DOL's Expansive View Of An Employee

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Law360, New York (July 22, 2015, 12:56 PM ET) -- Last week, the U.S. Department of Labor doubled down on its efforts to target the misclassification of workers through the issuance of guidance designed to clarify the test used to determine whether a worker is an employee or an independent contractor for purposes of federal wage-and-hour law. The end result is a more expansive reading of what constitutes an employee under the Fair Labor Standards Act and an unmistakable warning to employers that classify their workers as independent contractors, or consultants or freelancers or a variety of other categories, including those operating in the sharing economy.

The guidance, specifically a July 15, 2015, administrator's interpretation issued by Wage and Hour Division Administrator David Weil, reviews the various factors involved in determining whether a worker is an employee for purposes of the FLSA, and thus potentially entitled to minimum wage and overtime protections. While these factors are not new, the guidance discusses them in such a way as to make clear that the DOL leans heavily in the direction of employee when it comes to individual workers.

Although the administrator's interpretation does not itself carry the force of law, courts frequently give deference to agency interpretations when the law is not entirely clear. Indeed, the U.S. Supreme Court recently approved a 2010 administrator's interpretation by the DOL in Perez v. Mortgage Bankers Association. Employers should therefore be vigilant in ensuring that any independent contractors they use would not be considered employees. Indeed, employers that rely on an independent contractor business model should carefully review their worker classifications to ensure they are not at risk of an enforcement action or private litigation.

**Background**

In general, the FLSA itself is not particularly clear on how to distinguish between employees and nonemployees. The statute's definition of "employ" is given as "to suffer or permit to work" — a phrase that has spawned decades of case law and led to the development of the so-called economic realities test, which remains in use today.

Under this test, a worker's status is determined by reviewing the economic realities of his or her relationship with the employer. In the latest guidance as well as in previous interpretations, the DOL has generally distilled the economic realities test down to the question of whether the worker is economically dependent upon the business of the employer or is really in business for him or herself, and thus an independent contractor.

In order to determine whether such economic dependence exists, the test typically involves an evaluation of six different factors:

1. the extent to which the work performed is an integral part of the employer's business;
2. the worker's opportunity for profit or loss depending on his or her managerial skill;
3. the extent of the relative investments of the employer and the worker;
4. whether the work performed requires special skills and initiative;
5. the permanency of the relationship; and
6. the degree of control exercised or retained by the employer.

As the test is based on the totality of the working relationship, no one factor is dispositive. The test, therefore, is largely qualitative, and can lead to continued confusion for workers and employers about proper classification.

To make matters worse, not all courts apply the same factors under the economic realities test, which also applies to the Family Medical Leave Act, and there are numerous different tests with different factors and different emphases under various other state and federal laws, which are all applied slightly differently by both courts and agencies. Thus, a worker may be an independent contractor for some purposes, but not others. It is no surprise, therefore, that lawsuits and agency actions alleging improper classification of workers as independent contractors are on the rise, and employers are spending significant time and expense defending them.

**Administrator's Interpretation**

The issuance of the administrator's interpretation may have done little to clarify worker classification as a matter of law, since it in large part merely restates these well-known factors and summarizes how the law has developed in the area, albeit in a somewhat one-sided manner. However, the import of the guidance for employers is clear: The DOL is focusing on the increased use of independent contractors, including in the sharing economy, and the manner in which the DOL will use the economic realities test will result in an expansive view of what constitutes an employee.

This is stated both overtly, by concluding that "most workers are employees under the FLSA's broad definitions," and more subtly in the way that the DOL discusses and provides case law or real-world examples of each of the factors in the economic realities test.

For example, in discussing the factor of whether the work is an "integral part" of the employer's business, the DOL stresses that this factor is "compelling," defines it broadly to potentially include work that "is just one component of the business and/or is performed by hundreds or thousands of other workers" and concludes it is "unlikely" that a "true independent contractor's work ... [will] be integral to the employer's business."

In discussing the worker's relative investment compared to the employer's investment, the DOL takes the position that even "substantial" investments by the worker may be irrelevant if the employer's investment in its total business is more significant, suggesting that large companies could never satisfy this factor. Similarly, in discussing the "permanency of the relationship" factor, the guidance stresses that "a lack of permanence or indefiniteness does not automatically suggest an independent contractor relationship" and that the reason for it "should be carefully reviewed[.]"

Essentially, by discussing each factor in terms of how it can result in an employee classification, and by downplaying any inference or weight where such a factor leans toward independent contractor status, the administrator's determination sends the clear message that the DOL views most workers as employees, unless they are operating and holding themselves out as an independent business. Put another way, it would be difficult to use this guidance to confirm an independent contractor classification, but very easy to confirm an employee classification, and plaintiffs' attorneys will no doubt begin citing to it regularly in litigation.

**Conclusion**

Armed with this guidance, as well as its recent request for an additional $30 million in funding for 300 additional wage-and-hour investigators, employers should expect the DOL to enhance its focus on enforcement actions over independent contractors, including in the new sharing economy. In addition to other federal agencies, such as the National Labor Relations Board, states have also increased their enforcement efforts, including through audits, new laws, joint task forces and coordinated efforts with the DOL and IRS.

Finally, plaintiffs' attorneys are actively targeting employers that either misclassify workers or classify large percentages of their workforce as independent contractors, and both lawsuits and large settlements have been steadily increasing.

The consequences of misclassifying workers are enormous, and include back taxes, Social Security and Medicare taxes, unemployment insurance, workers' compensation, civil penalties, criminal penalties, government audits, back wages and liquidated damages, attorneys' fees and health insurance and benefits.

Given these substantial risks, prudent employers should, at a minimum: (1) regularly review and update internal processes and safeguards for hiring independent contractors; (2) review and strengthen independent contractor agreements and internal policies; (3) train managers on how to work with independent contractors; and (4) work with legal counsel to conduct privileged preventive audits.

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