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Worker Classification Continues As "Hot Topic" for 2024

BY ABBY M. WARREN AND JESSICA C. PINTO

On January 10, 2024, the US Department of Labor (DOL) published a final rule revising previous guidance on employee and independent contractor status under the Fair Labor Standards Act (FLSA) - a reminder for employers to ensure proper classification of workers. Misclassification poses serious risks to employers as it may deny workers proper protections and benefits and result in fines, penalties, payments, and other liability. Engineers may be susceptible to misclassification due to the varying nature of work among different sectors, contractual or project-based work, and remote work in different locations.

Generally, only "employees" are legally entitled to certain benefits and protections under most employment laws. Such benefits and protections may include rights to minimum wage, overtime pay, job-protected family and medical leave, anti-discrimination and anti-retaliation protections, workers' compensation, and unemployment insurance, among others. There are also certain record-keeping, authorization, and tax obligations for employers as it relates to employees. That being said, independent contractors are generally not entitled to such benefits and protections.

DETERMINING THE CLASSIFICATION

How do entities determine if a worker should be classified as an independent contractor versus an employee? There is a patchwork of tests used under various federal, state, and local laws by courts and government agencies. Various courts and agencies may focus on "common law" tests that emphasize an employer's degree of direction and control; "economic reality" tests that consider the level of economic dependence on the employer; strict elemental tests that require certain conditions to be met for independent contractor status; and other variations of tests. Common factors considered include the opportunity for profit or loss, investment, permanency, control, whether the work is an integral part of the business, and skill and initiative. Tests often afford little weight to an entity's characterization of the relationship - even if a written agreement specifies classification.

Constant changes and various iterations of classification tests are exemplified at the federal level. Since the 1940s, the DOL and courts applied an "economic reality" test to determine classification under the FLSA, with the DOL stating the ultimate inquiry as "whether, as an economic reality, the worker is dependent on the employer for work (and is thus an employee) or is in the business for themselves (and is thus an independent contractor)." Historically, the DOL and courts generally applied a totality-of-the-circumstances analysis with multiple factors, none necessarily controlling. Federal courts apply different iterations of this test, but often employ common factors.

The DOL published a rule in 2021, establishing five economic reality factors to gauge economic dependence, with greater weight given to two factors: (1) the employer's nature and degree of control over work; and (2) the worker's opportunity for profit or loss. The DOL replaced the rule with its current rule, effective March 11, 2024, stating it deviated from historical application. The DOL's new rule focuses on a multifactor "totality-of-the-circumstances" version of the economic reality test that does not apply predetermined weight to any factor, with the ultimate inquiry again being the degree of economic dependence. It remains unknown whether courts will apply this test.

Alongside the DOL's rule, classification tests differ across the map. For example, the California Supreme Court adopted the ABC test for classification under the California Wage Order. Under this test, a worker is only an independent contractor under the labor code if three conditions are met: the worker (A) is free from control and direction in regard to work; (B) performs work outside the usual course of the business; and (C) is customarily engaged in an independently established trade, occupation, or business of the same nature (with some exceptions). Other states and even some cities use a similar test under various employment laws (including Connecticut and Tucson, Arizona). These tests are also not static, as seen by the DOL's new final rule, rather, they change based on agency guidance, judicial interpretation, and changes in the law, creating further complication.

SIX KEY ACTIONS

Classifying workers is no easy feat. It is *important* for employers to understand the relevant test(s), their application, and the risks associated with misclassification as this area has been and continues to be a focus of enforcement. Therefore, as part of their compliance efforts, employers may wish to consider the following:

- **Know the Relevant Test(s)/Jurisdiction:** With remote work increasing and organizations hiring across jurisdictions, its crucial to determine which state and local laws and tests apply.
- **Conduct an Audit:** Conduct an audit of the workforce to determine if employees and contractors are properly classified.
- **Review Agreements:** Review current written designations, employment agreements, and contractor agreements to ensure they are accurate and consistent with the classification.
- **Focus on Training:** Train leaders, human resources personnel, and other individuals involved in hiring employees and engaging contractors on classification standards and issues.
- **Consider Your Organization's Goals:** Determine what the organization aims to achieve and what types of workers may best achieve those goals.
- **Consult with Legal Counsel:** Consult with legal counsel for assistance in compliance. *PE*

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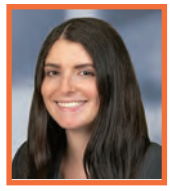

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