

Employee or Independent Contractor: Yet Another Test is Developed

BY FREDRIC MARCINAK

You don't have to be in business long before you start learning the differences between employees and independent contractors. For most purposes employees are entitled to benefits such as unemployment insurance, workers compensation, protection from discrimination, collective bargaining, etc., and employers must withhold taxes and make payroll tax payments for employees. Independent contractors, on the other hand, are usually not eligible for legal protections, are paid under a 1099 with no withholding, and often have contracts in place that allocate rights between the contracting parties. The employee-independent contractor distinction is an important one, especially in the transportation industry where independent contractors such as owner-operators have long played an important role. But the question of whether a worker is an employee or independent contractor is often not easy to answer. There are a variety of legal tests that are used, some employing a dozen or more factors, some used for one purpose—such as classification for tax purposes under federal law—but not for other purposes—such as classification for workers compensation eligibility under state law.

The United States Department of Labor has proposed yet another test—this time for determining eligibility for benefits under the Fair Labor Standards Act (FLSA). The FLSA is the federal law, in place since the 1930s, that regulates overtime, minimum wage, and working hours. Because the new test proposed by DOL applies only to FLSA eligibility, it will not impact entitlement to workers compensation, unemployment insurance, taxes, or other employment laws. But for FLSA purposes, the DOL proposes to adopt the “Economic Realities Test” that looks at five factors to determine classification:

1. The amount of control
2. The worker's opportunity for profit or loss based on their own merit
3. The skill involved
4. The permanence of the relationship
5. The integration of the work



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The DOL's proposal would make factors 1 and 2 the most important. If these factors favor either employee or independent contractor status, they will likely control the outcome. However, if these two factors conflict or are unclear, the remaining three factors will be considered. Thankfully, the DOL adds some clarity to the application of the first two factors. For example (and important in the trucking industry), control for safety purposes would not be considered too heavily because DOL wants to encourage safety regardless of classification and because many laws mandate safety for all personnel regardless of classification. Additionally, despite the fifth factor looking at "the integration of the work," the DOL's proposed test expressly disclaims a California-like ABC test that says a worker must be an employee if he is doing work of the same type as the company's work (e.g. an independent contractor driving trucks for a trucking company). Rather, the DOL's fifth factor will ask whether the worker could perform his activities independently of the company.

The DOL's new rule is only a proposal at this point. The public, including various trucking associations, will submit comments that will help shape the final rule. However, if something close to the proposed rule is adopted, the trucking industry will need to take note. Even though motor carriers enjoy an exemption from overtime claims under FLSA for interstate truck drivers operating under DOT hours of service regulations, the new DOL rule will impact drivers who do not cross state lines and operate only locally as well as other personnel such as some mechanics, sales people, office workers, and the like. As with other employee-contractor tests, a worker is not an independent contractor simply because she and the company agree she should be paid on a 1099. Instead, the company must look at the appropriate legal test to determine proper classification and to avoid stiff legal penalties that can arise from misclassification claims. Hopefully as the DOL test is finalized it will provide additional clarity for businesses across the country.