Client Alert: Department of Labor Seeks to Alter Independent Contractor Classification

BY TRACY THOMAS BOLAND AND BENJAMIN J. HINKS • OCTOBER 14, 2022

On October 13, 2022, the United States Department of Labor (DOL) published a proposed rule that seeks to alter the test for determining whether a worker is an independent contractor or an employee under the federal Fair Labor Standards Act (FLSA).

As a reminder, the FLSA imposes federal wage and hour requirements on employers with respect to their employees, including paying non-exempt employees minimum wage, compensating them for overtime for hours worked over 40 in a workweek, and complying with certain recordkeeping requirements. However, these requirements do not apply to independent contractors.

In January 2021, the Trump administration's DOL adopted employer-friendly regulations on worker classification. This included removing several considerations from the test that previously governed this issue and emphasizing two "core" factors for determining whether a worker was an independent contractor: (1) the degree to which workers had control over their work; and (2) the workers' opportunity for profit or loss.

By way of its proposed rule, the current DOL is seeking to replace the Trump-era test with its own, and in doing so make it more likely that workers previously classified as independent contractors must now be classified as employees. The proposed rule, if finalized, would largely restore the "economic reality test" that was in place during the Obama administration, which is more aligned with the factors traditionally weighed by the courts. The economic reality test considers the "totality of the circumstances" in determining whether a worker is "economically dependent on the employer for work or in business for themselves."

Specifically, the DOL proposes six factors to help determine proper classification, while noting that these factors may be non-exhaustive, and that no single factor is by itself determinative of worker classification. The enumerated factors are as follows:

1 – "OPPORTUNITY FOR PROFIT OR LOSS DEPENDING ON MANAGERIAL SKILL."

This factor assesses a worker's opportunity for profit or loss based on whether the worker exercises managerial skill that affects the worker's economic success or failure in performing the work. Specifically: whether the worker determines the charge or pay for the work provided (or at least can meaningfully negotiate it); whether the worker accepts or declines jobs or can meaningfully negotiate the order and/or time in which the jobs are performed; whether the worker engages in marketing, advertising, or other efforts to expand their business or secure more work; and whether the worker makes decisions to hire others, purchase materials and equipment, and/or rent space (as opposed

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to the amount and nature of the worker's investment). If these facts are true for a worker, it is more likely they are an independent contractor.

2 – "INVESTMENTS BY THE WORKER AND THE EMPLOYER."

A worker's investment indicates independent contractor status if the investment is capital or entrepreneurial in nature. The DOL states that "the worker's investment should generally support an independent business or serve a business-like function, such as increasing the worker's ability to do different types of or more work, reducing costs, or extending market reach." However, occasional "costs borne by a worker to perform a job are not capital and entrepreneurial."

3 – "DEGREE OF PERMANENCE OF THE WORK RELATIONSHIP."

This factor considers whether a work relationship is definite in duration or continuous. "[A]n indefinite or continuous relationship is consistent with an employment relationship, but a worker's lack of a permanent or indefinite relationship with an employer is not necessarily indicative of independent contractor status if it does not result from the worker's own independent business initiative." A work relationship that is definite in duration, non-exclusive, project-based, or sporadic, can indicate independent contractor status.

4 – "NATURE AND DEGREE OF CONTROL."

This factor considers control over scheduling, supervision over the performance of the work including the ability to assign work, set standards and discipline the worker, the worker's ability to work for others, as well as things like control over technology and economic aspects of work. If a worker does not maintain control over these aspects of their work, it indicates employee status.

5 – "EXTENT TO WHICH THE WORK PERFORMED IS AN INTEGRAL PART OF THE EMPLOYER'S BUSINESS."

This factor considers whether a worker performs a work function that is "critical, necessary, or central to the employer's principal business." If so, it indicates employee status. The DOL illustrates this factor with the example that a worker who picks tomatoes for a farm is more integral to the principal business of farming and therefore more likely to be an employee than someone who performs accounting services for the farm.

6 – "SKILL AND INITIATIVE."

This factor examines whether a worker utilizes "specialized skills" in performing their work and whether those skills "contribute to business-like initiative." If both are true, then the worker is more likely to be an independent contractor. However, if the work "does not require prior experience, the worker is dependent on training from the employer to perform the work, or the work requires no training," it indicates that the worker lacks specialized skills and is likely an employee.

The DOL stated that these six enumerated factors "are not to be applied mechanically but should be viewed along with any other relevant facts in light of whether they indicate economic dependence or independence."

KEY EMPLOYER TAKEAWAYS

- The issuance of this proposed rule should serve as a reminder that having a contract with a worker and labeling them an "independent contractor" does not necessarily mean they are one under the law. The worker must meet the statutory or regulatory test for being an independent contractor.
- The proposed rule would only alter the worker classification analysis for purposes of the FLSA. As such, a separate analysis would still need to be performed under any applicable state law. For instance, the Massachusetts Independent Contractor Law sets forth its own (incredibly stringent) three-pronged test for worker classification.

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The rule also would not alter the definition of contractor under other federal laws, such as the National Labor Relations Act.

- As a practical matter, the proposed rule would make it more likely that workers currently classified as independent contractors are misclassified. However, it is at present only a *proposed* rule and must proceed through the notice and comment period. If the DOL does finalize the rule, it is unlikely to happen before mid to late 2023.
- Employers have an opportunity to submit feedback or concerns about the proposed rule to the DOL. All comments must be submitted to the DOL by November 28, 2022.

Bowditch will continue to monitor and inform you of developments on this issue. Please contact your Bowditch lawyer with any questions.

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