Paradigm

INTERNATIONAL SOCIETY OF PRIMERUS LAW FIRMS

FALL 2015

A Global Stage

Primerus Helps Clients Thrive in a Global Marketplace

Current Legal Topics:

Asia Pacific
Europe, Middle East & Africa
Latin America & Caribbean
North America

Employers Beware: New DOL Interpretation Threatens to Require FLSA Coverage for Traditional Independent Contractors

Much has been made of the United States Department of Labor's ("DOL") proposed rule, promulgated in response to President Barack Obama's March 2014 Executive Order, that increases the standard salary level required for the Executive, Administrative and Professional "EAP" or "white collar" exemption under the Fair Labor Standards Act ("FLSA") from $455 a week ($23,660 for a full-year worker), to $970 per week ($50,440 per year). After all, it is estimated that over five million, currently exempt, salaried employees will be entitled to overtime pay if the Rule becomes final. However, the DOL's recent position[1] regarding its interpretation of the FLSA's "Suffer or Permit" employment definition has the potential, if upheld, to include coverage for as many or more individuals, who may otherwise be deemed independent contractors.

As of 2005, there was an estimated 10.3 million independent contractors working in the U.S.[2] The DOL maintains that many employees are misclassified as independent contractors.[3] The DOL contends that certain employers may be intentionally misclassifying employees to cut costs associated with workplace protections such as minimum wage, overtime compensation, unemployment insurance and workers' compensation. In addition, misclassification results in lower tax revenues for the government and creates an uneven playing field for employers who properly classify their workers.

On July 15, 2015, DOL Administrator David Weil issued his Administrator's Interpretation No. 2015-1 ("Interpretation No. 2015-1"). The DOL related that it continues to receive numerous complaints from workers alleging misclassification and continues to bring successful enforcement actions against employers who misclassify. It has pursued a multi-pronged approach, entering into memoranda of understanding with many states and the Internal Revenue Service, in an effort to share information to combat misclassification. Interpretation No. 2015-1 was issued to provide "additional guidance" to the regulated community in classifying workers and to curtail misclassification.[4]

The FLSA requires covered employers to pay time and a half to employees who work over 40 hours in a given work week.[5] Under the FLSA, "employee" is defined, with certain exceptions, as "any individual employed by an employer."[6] "Employer," in turn, is defined as including "any person acting directly or indirectly in the interest of an employee in relation to an employee…."[7] Under the FLSA, "'employ' includes to suffer or permit to work."[8]

The U.S. Supreme Court has noted that the FLSA's "employ" definition is broad and is derived from child labor statutes.[9] In addition, the Court noted, "'This Act contains its own definitions, comprehensive enough to require its application to many persons and working relationships, which prior to this Act, were not deemed to fall within an employer-employee category.'"[10] As

Morgan A. Godfrey

Morgan A. Godfrey is an attorney with more than 25 years' experience. He is a shareholder with O'Meara, Leer, Wagner & Kohl, P.A., where he chairs the firm's employment and labor law section. He is a frequent lecturer and author on a variety of employment law topics, including background investigations, employee misclassification, investigating complaints of discrimination, ADA and FMLA updates, and retaliation claims. He is a member of Primerus' Labor and Employment Executive Committee.

O'Meara, Leer, Wagner & Kohl, P.A.
7401 Metro Boulevard
Suite 600
Minneapolis, Minnesota 55439-3034

Phone: 952.806.0403
Fax: 952.893.8303

magodfrey@olwklaw.com
olwklaw.com

a result, the test applied to determine whether a worker is an employee or an independent contractor is the "economic realities test," rather than the common law "right of control"[11] standard.

The "economic realities test," also known as the *Silk*[12] test, considers the following factors: (1) the degree of control exercised by the employer over the workers; (2) the workers' opportunity for profit or loss; (3) the relative investment in the business; (4) the degree of skill and independent initiative required to perform the work; and (5) the permanence or duration of the working relationship.[13] No one factor is controlling nor is the list complete.[14] Several jurisdictions also include the extent to which the work is an integral part of the employer's business.[15]

Interpretation No. 2015-1 is not simply a regurgitation of existing law. It is clear that this 15-page document is an attempt to shape the analysis. First, it places high emphasis on whether the work performed is an integral part (e.g. painter working for painting company) of the employer's business. Concerning the opportunity for profit or loss factor, the DOL focuses less on whether the individual could be held to account for failing to perform and more on the individual's ability to use management skills to run and expand a business. In considering the relative investment factor, not only is the worker's investment important, but also the relative investment the worker has made compared to the hiring business. Worker investment in tools is downplayed. The DOL's focus on the fourth factor is not simply that the worker is skilled, but that they also display initiative similar to the management skills under the profit or loss factor. Concerning factor five, a permanent or indefinite relationship between worker and business suggests the worker is an employee. The "control" factor is downplayed. It must be more than theoretical; it must be actually exercised. Working from home or offsite, and employee control (flex schedules) over hours worked is not significant. The nature and degree of the alleged employer's control is key, rather than the employer's rationale. Finally, the DOL takes the position that the FLSA provides coverage where the worker is economically dependent, even if requisite control is not exercised.

If the DOL is successful in shaping the standards to be used in determining whether an individual is an employee or independent contractor, not only will there be greater exposure to businesses under the FLSA, but exposure will also be increased under the Family Medical Leave Act (FMLA), as the FMLA incorporates the FLSA's "employ" definition.[16]

The DOL's message is that businesses should review their relationships with those whom they contract. Red flags include situations in which individuals are employed in the same exact line the business is known for, those where the individual works solely for the one business and no other, those where the business exercises control (even quality control or following customer dictates), and those situations in which the individual has worked for the business on a permanent or indefinite basis.

1 U.S. Department of Labor and Wage Division, Administrator's Interpretation No. 2015-1, Administrator David Weil, July 15, 2015 ("Interpretation No. 2015-1").

2 See United States Government Accountability Office, Report to Ranking Minority Member, Committee on Health, Education, Labor, and Pensions, U.S. Senate, Employment Arrangements, Improved Outreach Could Help Ensure Property Worker Classification, p. 11, Table 2 (GAO-06-656 (July 2006)).

3 See generally, Robert I. Gosseen and Morgan A. Godfrey, Employee Misclassification: The Employment Law Issue *du Jour*, Paradigm October 2010.

4 Interpretation No. 2015-1 at p. 1.

5 29 U.S.C. § 207(a)(1).

6 *Id.* at § 203(e)(1).

7 *Id.* at § 203(d).

8 *Id.* at § 203(g).

9 *Rutherford Food Corp. v. McComb*, 331 U.S. 722, 728, 67 S.Ct. 1473, 1476 (1947).

10 *Id.* 331 U.S. at 729, 67 S.Ct. at 1476 (quoting *Walling v. Portland Terminal Co.*, 330 U.S. 148, 150, 67 S.Ct. 640 (1947)).

11 The "right of control" test included such factors as: (1) The right to control the means and manner of performance; (2) the mode of payment; (3) the furnishing of material or tools; (4) the control of the premises where the work is done; and (5) the right of the employer to discharge. See e.g. *Guhlke v. Roberts Truck Lines*, 281 Minn. 141, 143, 128 N.W.2d 324, 326 (1964). Of all factors, the right to control was considered the most significant. *Id.*

12 *United States v. Silk*, 331 U.S. 704 (1947).

13 Id. 331 U.S. at 716.

14 Id.

15 See e.g. *Brock v. Superior Care, Inc.*, 840 F.2d 1054, 1058-59 (2d Cir. 1988); *Secretary of Labor v. Lauritzen*, 835 F.2d 1529, 1535 (7th Cir. 1987). But see *Layton v. DHL Express (USA), Inc.*, 686 F.3d 1172 (11th Cir. 2012) (applying an eight factor test, which is a hybrid between the right to control test and the economic realities test).

16 29 U.S.C. § 1802(5) ("The term 'employ' has the meaning given such term under [the FLSA, 29 U.S.C. 203(g)]." See Interpretation No. 2015-1 at p. 2, fn. 3.