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## Are Your Workers Really Independent Contractors?

Many businesses classify some or all of their workers as independent contractors (who receive 1099s) rather than employees (who receive W-2s). The reason may be that the workers are truly independent contractors. However, the reason may be that the business is trying to avoid paying minimum wage or overtime pay, shift the financial burden of certain taxes to the worker, eliminate the obligation to pay unemployment insurance and eliminate the expense and perceived burden of workers' compensation.

The U.S. Department of Labor (the "DOL") has recently taken action to publicize its position that most workers are employees under the Fair Labor Standards Act (the "FLSA") and that businesses need to acknowledge that and bear the resulting burdens. In the DOL's opinion, misclassification of workers as independent contractors deprives the federal government of tax revenue it would otherwise receive and gives companies that improperly classify their workers as independent contractors an unfair competitive advantage over companies that properly classify their workers as employees.

The DOL believes that misclassification of workers as independent contractors also deprives workers of the protections that the FLSA was designed to provide. In the DOL's recent formal statement (Administrator's Interpretation No. 2015-1, issued July 15, 2015), the DOL clarified its view on distinguishing independent contractors from employees. The DOL's analysis applies to employee/independent contractor classifications under the FLSA, which address minimum wage, overtime pay, recordkeeping and youth employment standards affecting employees in the private sector and local, state and federal governments. Other employee protections, such as unemployment insurance, workers' compensation, entitlement to benefits under the Family and Medical Leave Act and entitlement to protections under the Occupational Safety and Health Act ("OSHA"), are also impacted.

The DOL analysis focuses on the "economic realities" test to determine whether a worker is properly classified as an independent contractor. The economic realities test turns on whether the worker is, viewed broadly, economically dependent upon the company or is in business for himself. The factors that the DOL will consider in applying the "economic realities" test include the following. However, no *one* factor will be determinative and all of the factors will be viewed in the context of whether they support economic dependence or independence.

**1. Is the work an integral part of the company's business?** If so, it is indicative that the worker is economically dependent upon the company and, therefore, an employee. A typical example is an Uber driver – the driver's role is central to Uber's business.<sup>1</sup> If I hire a service person to service my law firm's copying machine when service is necessary, the service

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<sup>1</sup> The appropriate treatment of Uber's drivers is in issue in several venues. The California Labor Commissioner held that an Uber's driver was an employee and, therefore, eligible for expense reimbursement, but that case is being appealed by Uber. There are other class action lawsuits pending in California, Florida and Massachusetts. If the "economic realities" test is the standard applied, however, it appears clear that Uber's drivers are employees.

person's role would not be integral to my law firm's business, nor would the service person be economically dependent upon me.

**2. Does the worker's managerial skill affect the worker's opportunity for profit or loss?** If not, it is indicative that the worker is economically dependent upon the company and, therefore, an employee. The focus is whether the worker, by using his managerial (or entrepreneurial) skill, can affect his opportunity for profit or loss. If the worker has the latitude to exercise his own judgment and use his initiative to generate a profit (or suffer a loss, if not), it is indicative that the worker is an independent contractor. The ability to increase the number of hours worked or the efficiency of the work is not a consideration. A typical example of an employee arrangement is certain commercial cleaning services – those workers who perform cleaning services for companies that train them to clean in a certain manner, find their clients, schedule their jobs, agree to the rates fixed by the companies and collect their revenue are more likely employees. However, if those workers marketed their businesses, found their own clients, scheduled their own jobs and negotiated and collected their own revenue, that would be more indicative of independent contractor status.

**3. How does the worker's relative investment compare to the company's investment?** This factor focuses on the nature and extent of the relative investments of the worker and the company. Tools and equipment necessary to perform a service or task are not taken into consideration. If the worker makes no investment or a minimal investment, thereby subjecting the worker to no risk of loss, the worker is likely not an independent contractor. However, if the worker markets for clients, leases space to meet with clients and store equipment and purchases equipment that would enable him to service additional clients, that would be indicative of independent contractor status, particularly if the investment is significant in comparison to the company's investment.

**4. Does the work performed require special skill and initiative?** A worker's business skills, judgment and initiative are the focus of this factor. However, the worker's technical skills necessary to perform the required work, regardless of how specialized (such as IT skills), are not taken into consideration. Workers providing carpentry services for clients obtained by the company with materials provided by the company and performed in accordance with the company's specifications and timetable would likely be employees. On the other hand, workers providing project-based carpentry services for a variety of clients obtained by them through their marketing efforts, with materials provided by them and performed when, where and how they determine are more likely to be independent contractors.

**5. Is the relationship between the worker and the company permanent or indefinite?** A relationship viewed as ongoing or continuous is more indicative of an employment relationship. A relationship that is not ongoing or continuous does not necessarily mean that a worker is an independent contractor, though. Certain industries or professions (such as nurses and non-medical caregivers) typically hire part-time workers or use staffing agencies on a regular basis; that structure would not be indicative of independent contractor status, as the worker is not using his initiative to obtain work through independent marketing. However, a nurse specializing in wound care who directly markets his services to clients for the limited period during which wound care services are necessary, negotiates his own rates and schedules his own time among several clients is more likely an independent contractor.

**6. What is the degree and nature of the company's control?** If the worker actually controls meaningful aspects of the work performed, it is indicative that he is an independent contractor. The ability to work remotely with little supervision and on the worker's own schedule

is not determinative, as technological advances and the global economy have facilitated telecommuting by employees. Although the DOL acknowledged that some companies have good reasons for exercising control over workers (such as regulatory requirements and/or to ensure customer satisfaction), those reasons would not be permissible exceptions for maintaining control. Therefore, if a company maintains control of meaningful aspects of the work performed, regardless of the reason, the control would make the worker more likely to be an employee. A nurse who performs services through a staffing agency in accordance with the staffing agency's training program, accepts the wages specified by the staffing agency and checks in and out of each job through the staffing agency's app is more likely an employee. A nurse who receives referrals from a staffing agency, negotiates his own wages and timetable with the client and performs the job utilizing his professional skills, rather than the staffing agency's training, policies and procedures, is more likely an independent contractor.

The bottom line is that if you have any workers that you have classified as independent contractors, it would be advisable to review your relationships by applying the "economic realities" test. If those workers are economically dependent upon you and their opportunity for profit or loss is not dependent upon their managerial (or entrepreneurial) skills, it would be advisable to properly classify them as employees and comply with the FLSA and other laws that are designed to protect employees. Properly reclassifying your workers as employees before the DOL (or one of the other federal or state agencies that cooperate or coordinate with the DOL<sup>2</sup>) audits you and before your worker suffers an injury for which you are not protected by workers' compensation will help you avoid significant headaches and expense.

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This article is intended for informational purposes only and does not constitute legal advice or establish an attorney/client relationship.

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<sup>2</sup> The DOL's analysis is not determinative for several other federal or state agencies, such as the IRS, which uses a 20-factor "control" test.