Schaffer Law, LLC
Labor and Employment Law

DOL Plans to Limit Exempt Status and Toughen Independent Contractor Enforcement

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The U.S. Department of Labor recently announced a proposal to expand the number of employees who would become eligible for overtime pay. Under the Fair Labor Standards Act ("FLSA") certain employees are exempt from overtime payments if they meet two key tests; the salary basis test, and the duties test. Under the salary basis test, an employee must currently earn at least $455 ($475 under Connecticut law) per week, and that salary may not fluctuate based on the number of hours worked, except in limited circumstances. In addition, the employee must also meet the duties test by showing they work in an executive, professional, or administrative position. Each type of position has a specific statutory definition. Outside sales representatives are also exempt, regardless of salary. Further, under federal law, computer employees meeting the salary test are exempt.

Under the Department's proposal, the salary test would not be satisfied unless the employee earns $970 per week ($50,440/year) versus the current $455 ($23,660). Also, a separate highly compensated employee exemption, which is not recognized in Connecticut, is currently met if the employee earns at least $100,000, regardless of the duties performed. The minimum earnings for the exemption would now increase to $122,148 per year. Both the highly compensated rate and the salary test rate would then increase annually based on inflation.

The government estimates that some 5 million additional employees will become non-exempt and eligible for overtime pay if the rule is implemented. This means that about 50% of

all current exempt employees would become overtime eligible, resulting in increased earnings of about 1 to 1.2 billion dollars more each year for such workers.

A prime motivating force for the change is the lack of real wage growth for a generation of employees. The current $23,660 rate places a family of four below the federal poverty level, and this is one way to move more people out of poverty conditions.

Independent Contractors

Separately, the USDOL issued an interpretation, No. 2015-1, which makes it tougher for employers to prove a worker is an independent contractor under the FLSA. Historically, the default position has been that workers are employees, unless the employer can prove independent contractor status. By classifying someone as an independent contractor the employer avoids the FICA match, tax withholding, unemployment taxes, workers compensation coverage, and the payment of minimum wages and overtime.

Traditionally, the courts have used the "economic realities test" to determine employment status under the FLSA. The test focuses on whether the worker is economically dependent on the employer, or is in business for himself. While the USDOL's interpretation continues to employ the economic realities test, it does so with an expansive reading of the FLSA's definition of "employ," which means "to suffer or permit to work." While the law's definition of "employ" has not changed, the USDOL has taken the position that the definition should be read very broadly, and suggests that most independent contractors today are improperly classified.

Given the USDOL's position, employers must now be able to prove:

1. The work done by the contractor is not an integral part of the employer's business;

2. The contractor's managerial skill impacts the possibility of not only profit, but also of loss. For example, the contractor's decision to hire others, purchase materials and equipment,

advertise, rent space, and manage time tables may reflect managerial skills that will affect the opportunity for profit or loss. Merely working more time to get the job done is not considered a managerial skill, but is more akin to a worker working overtime and would not be demonstrative of contractor status;

3. The investment made by the contractor goes beyond the specific job being performed for the employer, and should be in scale with that of the employer. In essence the contractor's investment should not be relatively minor compared to that of the employer.

4. The work requires special skill and initiative. Such skills must go beyond technical ability and also encompass the exercise of business judgment and initiative.

5. The relationship is not one of permanency or indefiniteness. A person truly in business for themselves normally does not work for a single customer on a continuous or repeated basis; and

6. That the contractor controls the meaningful aspects of the work and is viewed as conducting his own business.

While these elements have been relied on in the past under the economic realities test, the DOL's new approach begins with the assumption that the FLSA's definition of employment, "to suffer or permit to work" must be broadly applied when analyzing each element of the economic realities test to determine whether the worker is really in business for themselves, or is economically dependent on the employer. Employers should assume that proving independent contractor status will be more difficult in the future, and that the DOL will be much more aggressive in enforcing the law. In fact DOL and the IRS will now work together in a more coordinated effort, and DOL has requested $32 million additional dollars to hire 300 new enforcement officers and support staff.

Aside from these new federal developments, Connecticut employers must still meet a separate test, the ABC test, to pass muster under state law. The ABC test is comprised of three elements. Aside from proving the worker is customarily engaged in an independently established trade, occupation, profession or business of the same nature as the service being provided, the employer must also show the worker is free from direction and control in the performance of the service; and that the worker either performs services outside the usual course of the employer's business, or outside all of the employer's places of business. Arguably, this is an even tougher test to pass.

The bottom line is that employers should carefully review any independent contractor relationships it has and verify it can pass both tests, or be prepared to face aggressive regulatory action.

For more information contact scott@schaffer-law.com or (860) 216-1965.

www.schaffer-law.com