

Memo

From: Tammy McCutchen¹
Date: April 21, 2023
Re: Implementing AB5 under the Fair Labor Standards Act

Under Supreme Court precedent, “employees” under the FLSA are persons who “as a matter of economic reality are dependent upon the business to which they render service.” To determine economic dependence, federal courts and the DOL have considered different multi-factor balancing tests which have changed over time – sometimes five factors, sometimes six, sometimes seven; even similar factors are not quite the same from court to court and different courts balance the factors differently. The many different factor tests have prevented both businesses and workers from predicting who is an IC and who is an employee.

To reduce complexity, the Trump Administration issued the DOL’s first regulation on independent contracting on January 7, 2021, which gives the greatest weight to two core factors: (1) the nature and degree of control over the work, and (2) the worker’s opportunity for profit or loss. Only if those factors point in opposite directions, one showing independent contractor status and the other employment, would the DOL look at the three additional factors.

A Texas court ruled that the Biden Administration’s effort to withdraw the IC rule without replacing it was illegal. Thus, the Biden DOL now has proposed to return to a complex six-factor test. The proposal also adds “these six factors are not exhaustive,” “additional factors may be relevant” and “the weight to give each factor depend on the facts and circumstances of a particular case.”

In other words, as proposed, the DOL can consider any facts it wants and give those facts whatever weight it wants, including the “ABC test” of California’s AB5 law or the PRO Act – by fiat, without any notice or additional rulemaking.

The ABC test includes three required factors for ICs: (A) freedom from control; (B) performing work that is outside the usual course of business; and (C) being customarily engaged in an independent established trade, occupation, or business.

These three factors are within the DOL’s six factors, as shown in the chart below. Labor secretary nominee Julie Sue has not, will not, and cannot say that the three ABC factors are irrelevant to the economic dependence determination under the FLSA economic reality test. Neither has she said that the DOL **will not enforce** the proposed regulations to only consider these three factors or weigh them so heavily that no other factor matters.

No, the proposed regulations as written are not an ABC test. But it’s not about the specific language of the proposed rule; it’s about how the DOL will interpret and enforce that language. Nothing in the proposed regulations prevent the DOL from de facto applying the ABC test in any investigation to conclude that an IC has been misclassified. Few businesses have the resources to challenge the results of an investigation.

ABS's "ABC" Test	Proposed Biden Rule
(A) The person is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact.	Proposed § 795.110(b)(4) <i>Nature and degree of control</i> . This factor considers the employer's control, including reserved control, over the performance of the work and the economic aspects of the working relationship.
(B) The person performs work that is outside the usual course of the hiring entity's business.	Proposed § 795.110(b)(5) <i>Extent to which the work performed is an integral part of the employer's business</i> . This factor considers whether the work performed is an integral part of the employer's business.
(C) The person is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed.	Proposed § 795.110(b)(2) <i>Investments by the worker and the employer</i> . This factor considers whether any investments by a worker are capital or entrepreneurial in nature. . . . Investments that are capital or entrepreneurial in nature and thus indicate independent contractor status generally <i>support an independent business</i> and serve a business-like function . . . (emphasis added)

ⁱ Ms. McCutchen served as the U.S. Department of Labor's Administrator of the Wage & Hour Division during the George W. Bush Administration.