



NECA and IBEW Joint Comments on Employee or Independent Contractor Classification under the Fair Labor Standards Act

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The National Electrical Contractors Association (NECA) and the International Brotherhood of Electrical Workers, AFL-CIO, CLC (IBEW) submit these comments in support of the U.S. Department of Labor’s (DOL’s) Notice of Proposed Rulemaking (the Proposed Rule) on the standard for determining whether a worker is an employee or an independent contractor under the Fair Labor Standards Act (FLSA).¹

The IBEW is a labor organization representing approximately 775,000 active and retired members, including approximately 400,000 members working in the construction industry. These highly skilled and trained electricians play an integral role in construction projects of all types and sizes.

NECA is a national trade association and the leading voice of the \$202 billion electrical contracting industry that brings power, light, and communication technology to buildings and communities across the U.S. NECA collectively represents over 4,000 electrical contractor members served by 118 local chapters.

NECA members employ a unionized workforce with contracts collectively bargained with IBEW local unions. These collective bargaining agreements provide family-sustaining wages and benefits to employees while also facilitating compliance with labor and employment requirements such as workers’ compensation and unemployment insurance. Both IBEW and NECA members therefore have interest and expertise related to the impact of the Proposed Rule.

We applaud the DOL for issuing the Proposed Rule to overturn the flawed 2021 Independent Contractor Rule (2021 IC Rule), which would have particular impact in the construction industry. In these comments, we offer our shared perspective on how returning to the well-established “economic reality” test will benefit NECA members, IBEW members, workers and the economy by encouraging responsible employment practices and protecting workers.

I. Background

Employer misclassification of workers as independent contractors is a longstanding, pervasive problem affecting millions of workers and costing government agencies billions of dollars each year.² Misclassification is most common in industries where it is most profitable, such as construction, where workers’ compensation insurance premiums are substantial due to the inherent

¹ Notice of Proposed Rulemaking, “Employee or Independent Contractor Classification Under the Fair Labor Standards Act,” 87 FR 62218 (October 13, 2022).

² Lynn Rhinehart, et. al, *Misclassification, the ABC test, and employee status: The California experience and its relevance to current policy debates*, Economic Policy Institute (Jun. 16, 2021), <https://files.epi.org/uploads/229045.pdf>.

safety risks of working in the industry.³ The misclassification of construction workers is a significant problem that unfortunately often goes unchecked and without consequences, allowing unscrupulous employers to win construction contracts at the expense of taxpayers, responsible employers, and workers.

A. Congressional intent and judicial precedent support returning to the well-established six-factor “economic reality” test

The prior administration’s DOL finalized a rule that narrowed the scope of who is considered an employee under the FLSA. That rule stacks the deck against workers and enables employers to misclassify workers as independent contractors with no rights to minimum wage, overtime, or the protections of our child labor laws. It also contravenes the statutory definitions and Supreme Court precedent, which has recognized that the striking breadth and unique history of the FLSA’s definitions means that most workers are employees under the FLSA and entitled to the law’s protections. We applaud the DOL for proposing to undo this anti-worker rule and replace it with a rule that is consistent with the text and purposes of the FLSA and with judicial precedent.

The 2021 IC Rule’s divergence from the well-established common law approach to classifying workers under the FLSA would have created enormous confusion amongst the judicial system, employers, workers, enforcement officials, and private officials. The 2021 IC Rule would have also done away with over 70 years of DOL guidance⁴ instructing employers on how to navigate the FLSA.

The prior administration’s rule proposed a 5-factor test to determine the nature of a worker’s relationship with a business. In spite of decades of judicial precedent, the 2021 IC Rule identified two factors—the nature and degree of control over the work and the worker’s opportunity for profit or loss—as the “core factors” that carry the most weight in the analysis. The 2021 IC Rule also narrowed the facts to be considered under the “non-core” factors. In sum, the 2021 IC Rule criteria would make classification as an independent contractor easier to achieve for businesses looking to cut costs at the expense of workers and taxpayers. Determining employment status doesn’t depend on any one or two isolated factors. Rather, this analysis requires examining the totality of the circumstances of the relationship to determine the “economic reality” of whether the worker is economically dependent on the employer.

The FLSA’s employment standard ensures its protections extend to a wide range of workers. Congress established a broad definition of “employ” to include “to suffer or permit to work.”⁵ In using this definition, Congress unmistakably rejected the narrower common law test for employment, which turns on the degree to which the employer has control over an employee.⁶ In

³ *Id.* at 4.

⁴ *See, e.g.*, Administrator’s Interpretation (AI) 2015-1, “The Application of the Fair Labor Standards Act’s ‘Suffer or Permit’ Standard in the Identification of Employees Who Are Misclassified as Independent Contractors.”

⁵ 29 U.S.C. 203(g).

⁶ [T]he broad language of the FLSA, as interpreted by the Supreme Court . . . demands that a district court look beyond an entity’s formal right to control the physical performance of another’s work before declaring that the entity is not an employer under the FLSA.” *Zheng v. Liberty Apparel Co.*, 355 F.3d 61, 69 (2d Cir. 2003).

fact, employment under the FLSA’s “suffer or permit to work” standard is the “broadest definition that has ever been included in any one act.”⁷

The 2021 IC Rule does not accurately reflect the FLSA’s purpose and does not provide clarity for the stakeholders it impacts, including construction workers and construction employers. As discussed in the Proposed Rule, decades of judicial precedent exists applying the multi-factor “economic reality” test to determine when a worker is economically dependent on an employer.⁸ The ultimate question of economic dependence has, for decades, been evaluated by federal courts under the six-factor test articulated in the Proposed Rule.⁹ Courts look at the totality of circumstances, without assigning undue weight to any single factor or set of factors.¹⁰

B. Importance of returning to the six-factor “economic reality” test

NECA and IBEW support returning to the long-standing six-factor balancing test, which will ensure certainty and clarity for construction employers and employees, provide protection to law-abiding responsible contractors and workers in the construction industry, and reduce burdensome and costly litigation. The Proposed Rule will significantly reduce misclassification in the construction industry, which harms both construction workers and construction employers, and will provide clarity to employers regarding their legal and financial obligations.

NECA and IBEW support the DOL’s proposal to return to the original six-factor test under the Proposed Rule and additionally support its codification into the law. Unlike the 2021 IC Rule, the Proposed Rule is consistent with extensive judicial precedent. The Proposed Rule aims to ensure that *all of* the relevant factors are examined using a “totality-of-the-circumstances” approach, without assigning undue weight to a particular factor or set of factors.

The Proposed Rule’s six-factor “economy reality” test gets to the central issue: is the worker in business for themselves or do they depend on finding work in the business of others? DOL’s explanation of *how* each factor is analyzed for what it says about whether the worker is running an independent business also provides clarity and focus, which will help workers and businesses know who is covered. The proposed rule also makes clear that the vast majority of workers are not in business for themselves so are entitled to the FLSA’s rights and protections.

II. IBEW and NECA Recommendations

C. DOL should examine the effects of the 2021 IC Rule in the construction industry

We agree with DOL that “the misclassification of employees as independent contractors remains one of the most serious problems facing workers, businesses, and the broader economy.”¹¹ The Proposed Rule expressly reverses the 2021 IC Rule’s test and therefore dramatically shifts the rebalancing of the classification of workers under FLSA that favored independent contractor

⁷ United States v. Rosenwasser, 323 U.S. 360, 363 (1945) (*quoting* 81 Cong. Rec. 7,657 (1938) (remarks of Sen. Hugo Black)).

⁸ Tony & Susan Alamo Found. v. Sec’y of Labor, 471 U.S. 290, 301 (1985) (the test of employment under the FLSA is economic reality); Goldberg v. Whitaker House Co-op, Inc., 366 U.S. 28, 33 (1961).

⁹ Antenor v. D & S Farms, 88 F.3d 925, 932-33 (11th Cir. 1996).

¹⁰ Brock v. Superior Care, Inc., 840 F.2d 1054, 1059 (2d Cir. 1988).

¹¹ Proposed Rule, *supra* note 1, at 62225.

status. Therefore, we recommend that DOL include information in the final rule comparing the effects of the 2021 IC Rule to the Proposed Rule on various industries, particularly those where misclassification is common, including construction.

We urge DOL to pay keen attention to the effects of the 2021 IC Rule and drawing comparisons to the anticipated effects of the Proposed Rule in the construction industry, which constitutes a sizable economic sector that is poised for massive growth due the Bipartisan Infrastructure Law and other legislation incentivizing major construction projects. Specifically, we recommend that DOL:

- 1) Examine the increase in independent contractors in the construction industry and quantify the potential for lost wages that would result from the 2021 IC Rule. The 2021 IC Rule failed to estimate the number of workers who could be misclassified as a result of its proposal or address its impact on industries that experience rampant misclassification.
- 2) Quantify the benefits that workers would lose under the 2021 IC Rule, which would leave workers with fewer employer-provided benefits, such as health insurance and retirement contributions. The 2021 IC Rule failed to quantify these losses of benefits.
- 3) Quantify how the misclassification of workers impacts employer-funded insurance programs like workers' compensation and disability insurance, which are especially critical for construction workers who face significant workplace safety risks. The 2021 IC Rule failed to quantify these impacts.

Below, we review the ways in which misclassification harms workers and law-abiding employers in the construction industry.

a. Misclassification harms construction workers

Misclassification hurts employees in numerous ways, including many electricians, and often leads to low wages and little to no benefits, along with potential legal risks and serious tax implications for workers. Misclassification also cheats workers of fringe benefits, social insurance protection (Social Security, unemployment insurance, workers' compensation), labor protections (regarding safety/health and race, age, and gender discrimination), and union rights.

Construction workers are highly susceptible to misclassification because the typical business organization is such that the practice is easy to conceal, making employer responsibility more difficult to determine.¹² In addition, work is often project-based, temporary, performed at isolated, small, or scattered sites, and with multiple layers of contractors and subcontractors.

By making it easier for unscrupulous employers to misclassify, the 2021 IC Rule effectively weakens other key protections for workers that rely on the FLSA's definition of employment. Recent decades have seen the steady weakening of a number of key labor standards that once provided leverage and bargaining power for workers to improve job quality, including the rapid

¹² Françoise Carré, *(In)dependent Contractor Misclassification* at 6, Economic Policy Institute (2015), <https://files.epi.org/pdf/87595.pdf>

erosion of the federal minimum wage's purchasing power, rising wage theft, and more extensive misclassification of workers as independent contractors.¹³

While the implementation of the Proposed Rule will improve workplace standards for a broad array of workers, it will especially help people of color and immigrants who face unique barriers to economic security and often must accept low-wage, unsafe, and insecure working conditions, including work in industries where misclassification is common, i.e. the construction industry.¹⁴

Employees are also hurt by misclassification because it shifts the tax burden that should have been on the employer to the employee. Individuals classified as independent contractors are responsible for the payment of employment-based taxes that go toward Social Security and Medicare, currently 15.3% of earnings (IRS 2021). Employers are required to make the employer portion (50% of total FICA tax, i.e., 7.65% of wages) of these payments on behalf of employees. They also are required to pay premiums for unemployment insurance and workers' compensation coverage, as well as short-term disability benefits in some states. These costs, when combined with the cost of employee benefits, *can add as much as 30% or more to a worker's total costs*.¹⁵ These are substantial burdens placed upon the employee unknowingly when the person files their tax returns for the previous year.

b. Misclassification harms responsible construction employers

In the construction industry, misclassification is a cost-cutting tool used by unscrupulous contractors to cheat the system, shirk legal responsibility and tax obligations, and underbid law-abiding contractors to win both public and private construction projects.

When unscrupulous contractors misclassify their workers, responsible contractors' bids are undercut by 20-30 percent.¹⁶ Unscrupulous contractors can achieve these cost savings and more when they misclassify, including by violating minimum wage or prevailing wage laws, failure to pay legally required overtime pay, workers' compensation insurance, and more, resulting in significant harm to responsible employers, misclassified employees, and taxpayers.

Recent academic research confirms the competitive advantage contractors derive by misclassifying workers, as well as the costs misclassification imposes on workers and American taxpayers.¹⁷ This practice is rampant, with research showing that at least one-third of construction

¹³ Lawrence Mishel and Josh Bivens, *Identifying the policy levers generating wage suppression and wage inequality*, Economic Policy Institute (May 13, 2021), <https://www.epi.org/unequalpower/publications/wage-suppression-inequality/>.

¹⁴ Charlotte S. Alexander, *Misclassification and Antidiscrimination: An Empirical Analysis*, 101 Minn. L. Rev. 907, 924 (2017) (finding that in the construction industry, Hispanics or Latinos were overrepresented in the percentage of workers misclassified.) (internal citations omitted).

¹⁵ Lynn Rhinehart, et. al, *supra* note 2 at 4.

¹⁶ Françoise Carré, *(In)dependent Contractor Misclassification* at 5, Economic Policy Institute (2015), <https://files.epi.org/pdf/87595.pdf>. (“...the labor cost differential is estimated to range from 20 percent to 40 percent of payroll when employers do not pay the unemployment insurance tax, workers' compensation premiums, the employer share of Social Security, and pension or medical insurance.”)

¹⁷ See, e.g., Russell Ormiston, Dale Belman, and Mark Erlich, *An Empirical Methodology to Estimate the Incidence and Costs of Payroll Fraud in the Construction Industry* at 5 (2020), <https://stoptaxfraud.net/wp-content/uploads/2020/03/National-Carpenters-Study-Methodology-for-Wage-and-Tax-Fraud-Report-FINAL.pdf>.

workers in the U.S. South were estimated to be misclassified¹⁸ which indicates an environment of purposeful misclassification to remain competitive.

A 2014 analysis of payroll records for government-backed construction housing projects across 28 states found that “companies using stimulus money routinely snubbed labor law and the Internal Revenue Service by treating workers as independent contractors in a clear violation of what’s allowed.” These companies “listed workers as contractors instead of employees in order to beat competitors and cut costs,” allowing them to save “20% or more in labor costs” by misclassifying their employees.¹⁹

D. DOL should consider the economic risks of the 2021 IC Rule

The Proposed Rule would generate significant tangible and intangible benefits for responsible employers, workers, and taxpayers, thus promoting economic growth. DOL properly acknowledges this on a qualitative basis in the Proposed Rule. In the final rule, we urge DOL to develop more quantitative data comparing the economic benefits of the Proposed Rule against the economic risks posed by the 2021 IC Rule.

By making it easier for employers to misclassify their employees, misclassification poses significant financial risk to federal, state, and local governments due to billions in lost tax revenue. When employers misclassify employees as independent contractors, those workers do not receive the protections and benefits they are entitled to, and employers fail to pay taxes they are required to pay.

Misclassification imposes numerous costs on the economy and reduces tax revenues that could help fund important government programs.²⁰ Tax revenues are substantially impacted when misclassified workers fail to pay the correct taxes on their income.²¹ In the 1990s, approximately \$200 million per year was lost in unemployment insurance tax revenue during due to misclassification, and an estimated 80,000 workers per year entitled to unemployment insurance benefits did not receive them.²²

¹⁸ *Lots of Employees Get Misclassified as Contractors. Here’s Why It Matters.* (Jul. 5, 2017). Harvard Business Review. <https://hbr.org/2017/07/lots-of-employees-get-misclassified-as-contractors-heres-why-it-matters>.

¹⁹ Mishel and Bivens, *supra* note 12 (internal citations omitted).

²⁰ See Congressional Research Service, *The Tax Gap: Misclassification of Employees as Independent Contractors*, at 1 (Dec. 23, 2011), https://www.everycrsreport.com/files/20111223_R40807_f23bbc37cc588a74650a677be2a69_c4a49b1faa6.pdf.

²¹ Alexander, *supra* note 12 at 912-913 (“At least eleven states, three federal agencies, unions, journalists, and advocacy groups have conducted such studies, finding in New Jersey, for example, that ‘38 percent of employers were . . . misclassifying their workers and much, much higher rates of misclassification [were] found in certain industries,’ *particularly in construction*. Another report found misclassification rates of between thirteen and twenty-three percent in industries across eleven states, producing tax losses in the tens and hundreds of millions per state. Likewise, according to U.S. Government Accountability Office estimates, the last time the Internal Revenue Service conducted a comprehensive misclassification estimate, ‘the federal government lost out on \$2.72 billion in Social Security, unemployment, and income taxes because of employee misclassification.’”)

²² Lalith De Silva, et al., *Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs*, Planmatics, Inc. at 69 (prepared for the US Department of Labor Employment and Training Administration) (2000), <http://wdr.doleta.gov/owsdrr/00-5/00-5.pdf>.

The Internal Revenue Service (IRS) estimated that in 1984, roughly 15 percent of employers misclassified 3.4 million workers, costing the federal government \$1.6 billion in lost revenue,²³ which equates to \$3.72 billion in 2019 dollars. Nearly 60 percent of this lost revenue was attributable to misclassified workers failing to pay income taxes.²⁴

Construction employers that misclassify are able to evade such costs as FICA taxes, overtime pay, minimum wage laws, workers' compensation, unemployment insurance, and health and safety requirements. Allowing these bad actors to evade these costs does not 'level the playing field' amongst honest employers trying to compete for the same job.

II. Conclusion

NECA and the IBEW commend the Department for issuing the Proposed Rule to address the rampant misclassification across industries, particularly the construction sector. Worker misclassification hurts responsible contractors, workers, taxpayers and the economy as a whole.

The Proposed Rule will restore and provide greater clarity and consistency for employers and workers and provide an accurate evaluation of employment relationships consistent with congressional intent and judicial precedent. In addition, we believe it is critical to codify the six-factor test into the law to ensure that no future administration can disregard this well-established test for determining employment relationships.

The Proposed Rule will create a more level playing field and encourage responsible economic growth, averting the cascading effects of unsafe workplaces while making it more difficult for irresponsible employers to flout long established, well-meaning employment laws. NECA and the IBEW urge the Department to act expeditiously to adopt the Proposed Rule and include quantitative data on the ways it will benefit workers, responsible employers, and the economy.

²³ U.S. General Accounting Office, *Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention* at 10 (August 2009), <https://www.gao.gov/assets/gao-09-717.pdf>.

²⁴ *Id.* at 14.