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December 10, 2022

The Honorable Martin J. Walsh, Secretary of Labor
c/o Amy DeBisschop, Division of
Regulations, Legislation and Interpretation,
Wage and Hour Division, Room S-3502
U.S. Department of Labor,
200 Constitution Avenue, NW
Washington, DC 20210

Dear Mr. Secretary:

RE: Department of Labor Wage and Hour Division Notice of Proposed Rulemaking Titled "Employee or Independent Contractor Classification Under the Fair Labor Standards Act," RIN1235-AA43, 87 *Fed. Reg.* 62218 (October 13, 2022)

The National Federation of Independent Business (NFIB)[1] submits these comments in response to the notice of proposed rulemaking titled "Employee or Independent Contractor Classification Under the Fair Labor Standards Act" (NPRM) published by the U.S. Department of Labor (Department) in the Federal Register of October 13, 2022. The proposed rule would revise the Department's analysis for determining employee or independent contractor classification under the Fair Labor Standards Act (FLSA).[2] NFIB recommends and requests that the Department withdraw the NPRM and leave in

[1] NFIB is an incorporated nonprofit association representing small and independent businesses. NFIB protects and advances the ability of Americans to own, operate, and grow their businesses and ensures that governments of the United States and the fifty States hear the voice of small business as they formulate public policies.

[2] FLSA, 52 Stat. 1060 (June 25, 1938), as amended (codified at 29 U.S.C. 201-219).

place the Independent Contractor Rule (the 2021 Rule) promulgated by the Department in January 2021.[3]

Because small businesses seek the services of an efficient mix of employees and independent contractors to help grow their businesses, create jobs, control costs, and furnish goods and services at competitive prices in the free market, NFIB and its members have a substantial interest in the NPRM.

1. Background – Complexity of Independent Contractor Classification for Small Businesses

The issue of independent contractor classification has vexed lawmakers, administrative agencies, employers, and taxpayers for decades.[4] The independent contractor problem is one of definition since quite literally the term 'independent contractor' has a plethora of definitions. Frequently, employers must analyze worker status under three separate tests applied by different regulating agencies each with varying interpretations as to what constitutes an employer-employee relationship: the Internal Revenue Service (IRS); the Department of Labor, and state labor departments for purposes of unemployment compensation and state workers' compensation.[5] This fractured approach means that a worker might be an employee under a state labor department but an independent contractor under the IRS test, causing significant uncertainty for business owners. Analysis under just one multi-factored test can be challenging enough to say nothing of contending with two or more tests. The challenge is particularly acute for small business owners who must generally determine worker status without the benefit of outside legal counsel or even in-house human resource expertise. A small business owner's final determination on worker status can be a risky endeavor with abundant penalties for unintentional mistakes on legal interpretation.[6]

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[3] Final Rule, "Independent Contractor Status Under the Fair Labor Standards Act," 86 *Fed. Reg.* 1168 (January 7, 2021).

[4] *See* John Bruntz, "*The Employee/Independent Contractor Dichotomy: A Rose Is Not Always A Rose*", 8 Hofstra Lab. L.J. 337 (1991).

[5] 87 *Fed. Reg.* 62230, col. 3 through 62232 (discussing the common law control test as used by the IRS and the ABC test used by various states in the unemployment context). See also, Karen R. Harned, Georgine M. Kryda, and Elizabeth A. Milito, "*Creating a Workable Legal Standard for Defining an Independent Contractor*," 4 J. Bus. Entrepreneurship & L. Iss. 93 (2010).

[6] One commentator cleverly observed that, "former Supreme Court Justice Potter Stewart's famous comment concerning obscenity would seem to be equally applicable to the employee-independent contractor dichotomy – courts cannot provide a lucid definition, but they know it when they see it." Scott R. Swier and Molly E. Slaughter, "*The Employee/Independent Contractor Dichotomy in South Dakota for Unemployment Compensation and Workers' Compensation Purposes: An Examination and Suggested Analytical Framework*", 43 S.D. L. Rev. 56, 59-60 (1998).

As confusion over worker classification has ensued for decades, stakeholders increasingly have called for simplified analyses of worker status. A 1977 report to the Joint Committee on Taxation by the General Accounting Office (GAO), observed that under IRS rules "[w]ho may be classified [as] an employee as opposed to a self-employed person presently is not clear and is subject to conflicting interpretations . . . ."[7] In 1992, GAO revisited the issue of independent contractor status and reported that "rules for classifying workers are unclear and subject to conflicting interpretations. Therefore, distinguishing between the two types of workers can be difficult for businesses."[8] In 2009, GAO again looked at worker classification, but this time in the context of both IRS enforcement and at the Department. The report observed that "the tests used to determine whether a worker is an independent contractor or an employee are complex and differ from law to law."[9] Notably, the report's first option for addressing misclassification was to "[c]larify the distinction between employees and independent contractors under federal law."[10] In response to calls for clarity and refinement from Congress and other stakeholders, in 2020 the IRS compressed its 20-factor test into a three-pronged analysis based on the common law test.[11]

The Department heeded the call for modernization and refinement of independent contractor classification in 2021 when it issued the 2021 Rule that distinguishes between an employee and an independent contractor, applying a test of whether as a matter of economic reality, the individual is economically dependent on that employer for work or is in business for him-or herself.[12] To apply that test, an entity must, under the 2021 Rule, take into account five factors, with greater weight given to the first two: (1) the nature and degree of the individual's control over the work, (2) the individual's opportunity for profit or loss, (3) the amount of skill required for the work, (4) the degree of permanence of the working relationship between the individual and the potential employer, and (5) whether the work is part of an integrated unit of production.[13] The

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[7] "*Tax Treatment of Employees and Self-Employed Persons by the Internal Revenue Service: Problems and Solutions.*" GGD-77-88 at i (November 21, 1977), available at: https://www.gao.gov/assets/ggd-77-88.pdf.

[8] "*Approaches for Improving Independent Contractor Compliance*," GAO-GGD 92-108 at 1 (July 1992), available at: https://www.gao.gov/assets/ggd-92-108.pdf.

[9] "*Employee Misclassification*," GAO 09-717 at 3 (August 2009), available at: https://www.gao.gov/assets/gao-09-717.pdf.

[10] *Id.* at 33.n

[11] Publication 15-A Cat. No. 21453T Employer's Supplemental Tax Guide (Supplement to Pub. 15, Employer's Tax Guide) For use in 2020 https://www.irs.gov/pub/irs-prior/p15a--2020.pdf.

[12] 86 *Fed. Reg.* 1168 and codified at 29 C.F.R. § 795.105.

[13] 29 C.F.R. § 795.105(b).

2021 Rule emphasizes that actual practice is more relevant than what may be contractually or theoretically possible.[14]

2. The Current Independent Contractor Rule Provides a Clear Legal Standard and Benefits the Economy

NFIB generally supported the 2021 Rule as it clarifies and simplifies the economic reality test to the direct benefit of small businesses.[15] Consideration of two core factors – the nature and degree of the individual's control over the work and the individual's opportunity for profit or loss - better enables small businesses to make an accurate determination as to whether a worker is an employee or independent contractor under the FLSA.

Although no single factor, out of the five, is dispositive, the first two points are key to the analysis and are therefore afforded greater weight than the other factors.[16] Thus, if the first two factors are both in favor of one status or the other (employee or contractor), the remaining factors will, in most cases, not be considered. Moreover, when evaluating the individual's economic dependence on the potential employer, "the actual practice of the parties involved is more relevant than what may be contractually or theoretically possible."[17] The 2021 Rule, for example, states that a worker's theoretical ability to negotiate prices or to work for competing businesses is less telling if in reality they cannot perform work for others.[18]

The 2021 Rule's five-factor test eliminated some of the unnecessary complexity involved in making the determination between independent contractor or employee for purposes of the FLSA. Small businesses cannot afford the lawyers, accountants, and clerks that larger companies use to decipher complex regulations and draft and review contracts that account for ever-changing workplace rules. Instead, most small businesses engage in do-it-yourself compliance. But even as more workers look for the flexibility that comes with being self-employed, misclassification of independent contractors remains a significant risk for business owners. The 2021 Rule helps the

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[14] 86 *Fed. Reg.* 1203-1205.

[15] NFIB believes that the Department's first alternative remains a viable, and indeed beneficial option. As stated in the NPRM: "Codifying a common law control test for the FLSA could create a more uniform legal framework among Federal statutes, in the sense that entities would not, for example, have to understand and apply one employment classification standard for tax purposes and a different employment classification standard for FLSA purposes." 87 *Fed. Reg.* 62231, col. 1.

[16] 29 C.F.R. § 795.105(c).

[17] 29 C.F.R. § 795.110.

[18] *Id.*

small businesses of America by providing a test for classifying independent contractors that is simpler and easier to understand. The focus on the two "core" factors helps reduce uncertainty. Additionally, the 2021 Rule's clarification of the "integrated" factor of the economic reality test is significant in that its focus on the "integrated unit of production" better reflects present-day work arrangements.[19]

As the economy has evolved, businesses and individuals have found lower costs and increased satisfaction outside of traditional employment arrangements. The availability of independent contractors allows small businesses to be more flexible and more competitive. For instance, independent contractors can serve a variety of functions that are not easily performed by employees, such as a retail store that needs occasional IT support for its website. Independent contractors offer small businesses a skill that is needed by the business for a short period of time or on an occasional basis. Contrary to what many in the labor movement believe, small business has no interest in turning every employee into an independent contractor. On the other hand, an increasing number of self-employed persons desire to reap the benefits of becoming an independent contractor.

Overall, the 2021 Rule's focus on two core factors provides small business employers and independent contractors clarity on when employee status will attach to a relationship between a business and worker. This offers employers and independent contractors greater predictability and stability thereby encouraging small business expansion and new business formation.

3. The Department's NPRM Will Adversely Affect the American Economy

Without a discussion of how the 2021 Rule has failed, the Department wishes to abandon the 2021 Rule and offers the NPRM, which would result in increased uncertainty, greater compliance costs, and more litigation. Such a reversal would be an unfortunate blow to small business owners and the American economy.

Under the NPRM, the Department would return to a "totality of the circumstances" analysis to evaluate the economic realities of the relationship between a worker and a company.[20] As a rationale for the NPRM, the Department emphasized that independent contractors are those workers who are not economically dependent on their employer for work and are in business for themselves. To determine economic dependence, the NPRM generally reverts to a six-factor economic reality test, but with some unfortunate added enhancements. According to the Department, these factors are simply "tools" or

[19] 29 C.F.R. § 795.105(d)(2)(iii).

[20] 87 *Fed. Reg.* 62274, col. 3 (setting forth the Department's proposed 29 C.F.R. § 795.110: "These factors are tools or guides to conduct a totality-of-the circumstances analysis. This means that the outcome of the analysis does not depend on isolated factors but rather upon the circumstances of the whole activity to answer the question of whether the worker is economically dependent on the employer for work or is in business for themself.").

"guides" to evaluate the totality of the circumstances. A determination as to whether a worker is properly classified as an employee or as an independent contractor will be based on the larger picture of whether the worker is economically dependent.

The NPRM would also abandon the use of two "core factors" and return to a "totality-of-the-circumstances analysis" using six factors.[21] The Department said it would return to an interpretation of the economic reality factors without assigning a predetermined weight to a particular factor or set of factors. The six factors set forth in the NPRM[22] are:

1. The worker's opportunity for profit or loss depending on managerial skill;[23]
2. The relative amount of investment made by the worker in comparison to investments made by the potential employer (the NPRM states that worker costs incurred for tools and equipment to perform specific jobs do not count as an investment and "indicate employee status");[24]
3. The permanency of the worker's relationship with the potential employer (the NPRM states that a work relationship that is "definite in duration, non-exclusive, project-based, or sporadic" indicates a contractor relationship);[25]
4. The nature and degree of the potential employer's control (the NPRM states that control exercised by the potential employer for compliance with "legal obligations, safety standards, or contractual or customer service standards" could indicate an employee relationship);[26]
5. The extent to which the work performed is an integral part of the potential employer's business;[27] and
6. Whether the worker uses specialized skills indicative of business-like initiative.[28]

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[21] 87 *Fed. Reg.* 62272, col. 1.

[22] 87 Fed. Reg. 62274-62275 (setting forth the Department's proposed 29 proposed 29 C.F.R. § 795.110).

[23] 87 *Fed. Reg.* 62274, col. 3 (the Department's proposed 29 C.F.R. § 795.110(b)(1)).

[24] 87 *Fed. Reg.* 62275, col. 1 (the Department's proposed 29 C.F.R. § 795.110(b)(2)).

[25] 87 *Fed. Reg.* 62275, col. 1 (the Department's proposed 29 C.F.R. § 795.110(b)(3)).

[26] 87 *Fed. Reg.* 62275, col. 2 (the Department's proposed 29 C.F.R. § 795.110(b)(4)).

[27] 87 *Fed. Reg.* 62275, col. 2-3 (the Department's proposed 29 C.F.R. § 795.110(b)(5)).

[28] 87 *Fed. Reg.* 62275, col. 3 (the Department's proposed 29 C.F.R. § 795.110(b)(6)).

In addition, the NPRM states that "additional factors" that "may be relevant" should also be considered.[29] This means the Department's proposal goes beyond the prior six-factor economic reality test and adds a seventh [unspecified] factor that the Department may also consider "additional factors" beyond the six, if they indicate the worker may be in business for themselves.[30]

A return to six factors, plus a potential undefined seventh factor, would make it more difficult for businesses to determine whether an individual is properly classified as an independent contractor—putting businesses who hire consultants, contractors, and individual entrepreneurs at risk of liability from misclassification. This would be unfortunate for America's small businesses that depend on independent contractors to carry out critical work roles, particularly considering recent labor shortages. Even before the pandemic, workers sought the flexibility that an independent contractor relationship provides. A 2018 Bureau of Labor Statistics Contingent Worker Survey found that less than one out of every ten independent contractors would prefer traditional employment status.[31] Companies, however, will be less likely to engage a contractor or consultant if there's uncertainty over a worker's status since a finding of misclassification can result in ruinous penalties, such as unpaid overtime and minimum wage, liquidated damages, and attorneys' fees.

The NPRM's rescission of the refined 2021 Rule would cause more legal uncertainty for workers and businesses who enter independent contracting relationships. This means less job growth and less new business creation. One fails to see how the Department's proposal, which would stifle an entrepreneurial economy, fits within the Administration's calls to support small business as just last year, President Biden proclaimed:

> Small businesses are the engines of our economic progress; they're the glue and the heart and soul of our communities. But they're getting crushed. Since the beginning of this pandemic, 400,000 small businesses have closed – 400,000 – and millions more are hanging by a thread. . . .These small businesses – not the ones with 500 employees, but these small businesses that, with a handful of folks, they are 90 percent of the businesses in America.[32]

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[29] 87 Fed. Reg. 62235, col. 3.

[30] 87 *Fed. Reg.* 62275, col. 3 (the Department's proposed 29 C.F.R. § 795.110(b)(7)).

[31] *See* U.S. Bureau of Labor Statistics, Contingent and Alternative Employment Arrangements table 11 (June 7, 2018), available at https://www.bls.gov/news.release/pdf/conemp.pdf.

[32] White House, "Remarks by President Biden on Helping Small Businesses" (February 22, 2021), available at https://www.whitehouse.gov/briefing-room/speeches-remarks/2021/02/22/remarks-by-president-biden-on-helping-small-businesses/.

Instead of helping small businesses, the engines of our economy "grow and compete,"[33] as President Biden has charged his Administration, the NPRM would directly harm America's small businesses that, according to the White House, "account for 44 percent of U.S. GDP, create two-thirds of net new jobs, and employ nearly half of America's workers."[34] To remain faithful to President's Biden's 2021 and 2022 statements, and to help the small businesses and entrepreneurs that are crucial to America's economy, the Department should withdraw the NPRM and leave in place the 2021 Rule.

4. The Department Should Issue a Supplemental Executive Order 13563 Analysis and a Supplemental Regulatory Flexibility Analysis to Take Proper Account of Costs the NPRM Would Impose on Small Businesses

NFIB encourages the Department to conduct and publish for comment, before it proceeds to a final rule, a thorough, supplemental Initial Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. 601-612) to take proper account of the potential impact of the rule proposed by the NPRM on small businesses. The initial analysis published in the NPRM did not take full account of the costs the proposed rule would impose on small businesses and offers disputed benefits. First, the Department estimates that it will only take employers 30 minutes to gain familiarity with a new independent contractor rule and it will take independent contractors just 15 minutes to get a handle on the regulation.[35] NFIB believes it will take many employers and contractors hours instead of minutes to digest a new rule and any subsequent subregulatory guidance.[36]

Secondly, NFIB questions whether many of the cited "benefits" of the NPRM would in fact benefit small businesses (i.e., transfer of "employer-provided fringe benefits" and prevention of "increased burden on government entities").[37] And, as noted above, NFIB does not believe that the NPRM will result in "reduced misclassification," another cited benefit of the NPRM.[38] To the contrary, adding to rather than simplifying the analysis of worker status creates more uncertainty and opportunity for misclassification error. This will cause small businesses to incur greater insurance and legal costs because of

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[33] White House, "A Proclamation on National Small Business Week, 2022" (April 29, 2022), available at https://www.whitehouse.gov/briefing-room/presidential-actions/2022/04/29/a-proclamation-on-national-small-business-week-2022/.

[34] White House Fact Sheet: Biden-Harris Administration Increases Lending to Small Businesses in Need, Announces Changes to PPP to Further Promote Equitable Access to Relief (February 22, 2021), available at https://bit.ly/3Y3lGgK.

[35] 87 *Fed. Reg.* 62266, col. 2.

[36] 87 Fed. Reg. 62273, col. 1 (the Department acknowledges that in addition to a new rule, small entities would incur additional costs to familiarize themselves with any subregulatory guidance).

[37] 87 *Fed. Reg.* 62267-62268.

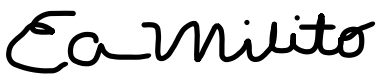
[38] 87 *Fed. Reg.* 62266, col. 3.

increased exposure under the NPRM to allegations of wage and hour violations by contractors and agency enforcement for whom the proposed rule makes the small businesses employers. The Department should ensure that it discloses to the public for comment, and that it fully considers in the rulemaking process, all costs its proposed rule would impose on small businesses.

Conclusion

NFIB recommends and requests that the Department withdraw its notice of proposed rulemaking "Employee or Independent Contractor Classification Under the Fair Labor Standards Act" published in the Federal Register October 13, 2022. The success of the American economy depends on the success of America's small businesses. And the success of America's small businesses depends in part upon clearer and less burdensome federal regulations. The 2021 Rule provides a standard under the FLSA that is more predictable and workable for America's small businesses.

Sincerely,



Elizabeth A. Milito, Esq.
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Approved for filing:

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