

Insights

U.S. Department of Labor Proposes Return to 2021 Independent Contractor Standard

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DOL's New Proposal to Distinguish Employees from Independent Contractors

On February 27, 2026, the U.S. Department of Labor (DOL) issued a Notice of proposed rulemaking to redefine independent contractor status under the Fair Labor Standards Act (FLSA). The proposed rule would also apply to the Family and Medical Leave Act (FMLA) and the Migrant and Seasonal Agricultural Worker Protection Act (MSPA), which incorporate the FLSA's definition of "employee." The proposed rule is not yet final. Public comments are open through April 28, 2026.

Out with Narrow Definition of Independent Contractors

The proposed rule would replace the 2024 Biden-era regulation with a modified version of the 2021 framework for determining worker status under the FLSA. Although the 2024 rule has not been formally rescinded, since May 1, 2025, the DOL has instructed its investigators not to apply the six-factor "totality-of-the-circumstances" test from the 2024 rule:

1. Worker's opportunity for profit or exposure to loss.
2. Respective investments by the worker and employer.
3. Permanence of the work relationship.
4. Nature and degree of control.
5. Whether the type of work is an integral part of the employer's business.
6. Skill and initiative applied by the worker.

Core Legal Framework: The Economic Reality Test

The proposed rule will likely increase the number of workers lawfully classified as independent contractors. It proposes a more permissive classification standard that centers on the "Economic Reality Test," giving primary weight to two factors:

1. **Nature and degree of control** – the extent to which the company controls how, when, and where work is performed, including scheduling, exclusivity, and economic terms. Greater control suggests employee status.
2. **Opportunity for profit or loss** – whether workers can meaningfully influence earnings through business decisions, such as setting rates, marketing services, hiring assistants, or making investments. Earnings limited to assigned hours favor employee status; entrepreneurial discretion favor independent contractor status.

Other factors --- such as skill required, permanency of relationship, and integration into the business --- remain relevant but carry less weight. The DOL stresses that actual working practices outweigh contract labels.

Important State-Level Differences

Employers must be aware that worker classifications may differ between federal and state law. State agencies apply their own statutory and regulatory tests and are not required to follow the DOL's revised framework, IRS guidance, or other federal standards when determining worker status for state unemployment insurance purposes.

The Indiana Department of Workforce Development (IDWD) applies a “direction and control” test derived from the Indiana Unemployment Compensation Act, which presumes that services performed for remuneration are employment unless the worker is free from direction and control both contractually and in practice. IDWD may thus classify a worker as an employee even if the worker meets the DOL standards for independent contractors.

The Illinois Department of Employment Security (IDES) applies the Illinois Unemployment Insurance Act's strict “ABC Test” of an independent contractor, which requires the employer to prove (A) Absence of control, (B) Business outside the usual course of the company's business, and (C) Customary engagement by the worker in an independently established trade. Failure to satisfy any one element of the ABC test results in employee status for unemployment insurance purposes, even if the worker qualifies as an independent contractor under federal law.

Companies must be mindful of these state standards or face exposure to state-level enforcement actions, including interest and monetary penalties.

What This Means for Businesses

- **Reevaluate classifications:** Review worker classifications under the relaxed federal framework, keeping in mind that state standards may not align and that actual practices matter more than the language of an independent contractor agreement.
- **Reduced litigation risk:** The standard under the proposed rule will decrease the risk of federal enforcement actions for misclassifying workers as independent contractors.
- **Next steps:** Public comments are due by April 28, 2026. If finalized, the proposed rule will apply to worker classifications under the FLSA, FMLA, and MSPA, but state law requirements will remain independently enforceable.

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