

NJDOL ABC Rule Adoption Spells Trouble for NJ Companies Using an Independent Contractor Model

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New Jersey businesses which use a 1099 independent contractor model for their workers were delivered an unwelcome package by the New Jersey Department of Labor (DOL) on May 5, 2026, when the department enacted its final rule to enshrine the employee-favorable ABC test into law. Employers may have been lulled into thinking the rule, first drafted a year ago in May 2025 and mostly on ice since then, would never arrive. But it did. The rule was implemented with the deletion of certain controversial provisions from its original draft, but which still tilts heavily against independent contractors. This rule now gives labor enforcement officials the strongest hammer yet to nail employers who skirt the W2 model.

New Jersey employers should know that the ABC test is not new, and it was not created by these new regulations. It has been part of the New Jersey Unemployment Compensation Law for some 90 years. Moreover, eleven years ago in *Hargrove v. Sleepy's*, 220 N.J. 289 (2015), the New Jersey Supreme Court extended the ABC test to both the New Jersey Wage and Hour Law and the New Jersey Wage Payment Law. Thus, the ABC test has already been the law for some



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time. What is new are the regulations which codify and explicate the elements of the test.

The legal implications of the ABC test are immense and rank among the more commonly misunderstood concepts in our legal system. With employees, companies must provide statutory paid leave, contribute to unemployment insurance, pay local, state, and federal wage taxes, comply with applicable minimum wage and overtime laws, and provide paid sick leave and healthcare benefits, among other benefits. Under State law, New Jersey employers are required to maintain payroll and wage records (inclusive of hours worked, earnings, deductions

and other required employee information) for six years or be subject to financial penalties. Also, employees are permitted to unionize, whereas true contractors are not. Businesses can face steep fines for using a 1099 model when it is not warranted by the facts. New Jersey has one of the strongest labor enforcement teams in the country, securing millions from businesses caught using the incorrect worker model.

The ABC test is the strictest of the various tests for determining whether a worker is an independent contractor excluded from a raft of benefits, or an employee covered by those same benefits. Under the ABC test, as a default, a worker is considered an employee and only proven otherwise as an independent contractor if they satisfy all three of these elements: free from control or direction over the performance of services; the work is performed outside the usual course of the business or outside the enterprise's place of business; and the worker is customarily engaged in an independently established trade, occupation, profession or business. The ABC test had been a test shaped by the state courts.

As noted in the DOL's response to comments to its proposed rule, the term "employment" has been defined under unemployment law broadly to include "any service performed for remuneration or under any contract of hire, written or oral, express or implied. N.J.S.A. 43:21-19(i)(1)(A)." Once it is established that a service has been performed for remuneration, that service is deemed to be employment, unless and until it is shown that all of these are present: (A) Such individual has been and will continue to be free from control or direction over the performance of such service, both under his contract of service and in fact; and (B) Such service is either outside the usual course of the business for which such service is performed, or that such service is performed outside of all the places of business of the enterprise for which such

service is performed; and (C) Such individual is customarily engaged in an independently established trade, occupation, profession or business. N.J.S.A. 43:21-19(i)(6).

Under the proposed rules, to determine control and direction over the worker under Prong A, the DOL looks at whether the employer has the right to control the details and means by which the services are performed by the worker, including requiring the individuals to use certain tools, wear a uniform displaying a logo/insignia and report on any aspect of the worker's services at prescribed times or intervals. However, the DOL is no longer considering actions to comply with federal, state or local laws and regulations, in and of itself, as evidence of control or direction.

When determining whether the work is outside the usual course of business for which the service is performed, in Prong B, the DOL explained that per its revised rules, a personal residence where an individual performs remote work, will not be considered among the employer's places of business. Similarly, in determining whether a worker is customarily engaged in an established occupation, profession or business, in Prong C, under the new rules, the agency will not focus on if the worker actually performed work for others other than the contracted entity, but rather if the worker is free and able to perform work for other entities.

Some see this enactment as the latest step by New Jersey to pull away the welcome mat for independent contractors and ramp up enforcement in the state. True independent contractors enjoy flexibility in work hours and work selection that employees may not enjoy. They control when, where, and how they do their work and for whom they work. For workers who enjoy remote work, being an independent contractor would guarantee that benefit over employees who are, at times, compelled to work in an office. They may have greater opportunities for income

growth due to multiple and more frequent contracts. While a company decides the product or service to be delivered, the independent contractor gets to choose the means for delivering the product or service. They can develop skills that put them in high demand. While contractors are not covered by an employer-provided health insurance plan, they may prefer to shop in the healthcare marketplace and choose from a variety of plans.

Given the differences in employment benefits, the quandary becomes deciding whether an independent contractor arrangement is legitimate or not. States use various tests—including the common law or economic realities tests—to determine whether a worker is legally an independent contractor or an employee. Other states are also more favorable for an independent contractor model with some embracing independent contractors and other alternate forms of worker participation as a way of attracting new businesses.

Now, there is no longer a doubt that New Jersey's rule is designed to categorize workers, as a default, even those with entrepreneurial aspirations, into employee status.

During the comment period, many companies weighed in against the draft rule. The final rule codifying a three-prong ABC test does not contain some of the more controversial aspects of its proposed version, such as the list of examples published in the original draft where workers would not be deemed independent contractors. Substantively, the law still heavily favors employee status as the default in its analysis.

Misclassifying workers as independent contractors when the test is not met can subject an entity to serious sanctions in addition to the full

panoply of benefits and taxes required to have been paid as an employer.

According to the Department of Labor, this rule consolidates decades of legal precedent—including key New Jersey Supreme Court rulings—and applies across statutes such as the Unemployment Compensation Law, Wage and Hour Law and Wage Payment Law. State officials note that the implementation of the rule reduces ambiguity and adds certainty to work classification. It certainly makes enforcement expectations more transparent. Under this rule, only bonafide independent contractor arrangements will pass muster. The regulation is expected to be published June 1, 2026. It will take effect on Oct. 1, 2026, following a 120-day phase-in period. The 120-day stay until the rules become effective may lead to more jockeying by businesses advocating for interim legislation hoping to avoid the expected increase in scrutiny of worker arrangements.

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