insights

SHUMAKER
Shumaker, Loop & Kendrick, LLP

A Newsletter from Shumaker, Loop & Kendrick, LLP | June 2016

TO SUFFER OR PERMIT:
How The Broad Scope Of The Fair Labor Standards Act Is Increasing The Risk Of Doing Business

2016 is shaping up to be a troubling one for employers subject to the provisions of the Fair Labor Standards Act ("FLSA"), 29 U.S.C. 201, *et seq*. In addition to the Department of Labor's ("DOL") revisions to the FLSA's white collar exemptions, which will go into effect on December 1, 2016 [see article on page 8], the DOL also recently issued Administrator's Interpretation No. 2016-1 ("AI") addressing the concept of "joint employment" under both the FLSA and the Migrant and Seasonal Agricultural Worker Protection Act ("MSPA"), 29 U.S.C. § 1801, *et seq*. This new guidance, which uses an "economic realities" standard to analyze the potential joint employment relationship, represents a stark departure from the common law control standard frequently utilized by courts. Because the economic realities standard is much broader than that of control, the AI has significant and detrimental implications for businesses that contract with third parties, such as staffing agencies, for workers or administrative functions, or for those that share employees with associated entities.

by Kate Decker

and Mechelle Zarou

The AI addresses two primary issues: the broad scope of employment relationships under the FLSA and the MSPA, and the standard for determining potential joint employment relationships. We will analyze both portions of the AI, and address the implications for affected employers.

The Broad Definition of Employment Under the FLSA and MSPA

The broad scope of the FLSA is evident in its definitions. For instance, the FLSA defines an "employee" as "any individual employed by an employer;" 29 U.S.C. § 203(e)(1); and an "employer" as "any person acting directly or indirectly in the interest of an employer in relation to an employee;" 29 U.S.C. § 203(d). Further, the FLSA defines the term "employ" as "to suffer or permit" to work, a definition that the MSPA adopts. 29 U.S.C. § 203(g). This definition does not require consideration of the level of control exerted by the putative employer, as the common law does. Instead, this definition rejects the common law control standard, and anyone who suffers or permits another to work is a statutory employer. The DOL thus concludes that this definition of "employ" is the broadest definition to ever be included in a statute.

The DOL next asserts that joint employment – as contemplated by the FLSA regulations – should be construed just as broadly, based on these broad definitions, which omit consideration of the narrower common law control standard. Notably, the DOL states that, "courts have found economic dependence under a multitude of circumstances where the alleged employer exercised little or no control or supervision over the putative employees."[1] Under the FLSA and MSPA definitions, this economic dependence is the most important factor in finding joint employment exists, far

more important than the exercise of control. Further, given the shared definition of employment between the two statutes and coextensive scope of joint employment between them, it is appropriate to rely on both statute's regulations to determine whether a joint employment relationship exists in a case arising under either statute.

If the intermediary employer is not an actual employee of the potential joint employer, the DOL requires that the vertical joint employment inquiry proceed to its second step – the "economic realities" analysis.

Types of Joint Employment

The AI distinguishes between two types of potential joint employment. The first type, horizontal joint employment, "exists where the employee has employment relationships with two or more employers and the employers are sufficiently associated or related with respect to the employee such that they jointly employ the employee."[2] The second type, vertical joint employment, "exists where the employee has an employment relationship with one employer (typically a staffing agency, subcontractor, labor provider, or other intermediary employer) and the economic realities show that he or she is economically dependent on, and thus employed by, another entity involved in the work."[3] Each type of joint employment is subject to its own analysis, which we outline below.

Horizontal Joint Employment

The DOL explains that the typical hallmark of a horizontal joint employment situation is an established employment relationship between an employee and various employers pursuant to which the employee usually performs separate work and works separate hours for each employer, where the employers are "sufficiently associated"[4] to be joint employers. Examples of potential horizontal joint employment scenarios include a waitress who works for separate restaurants that are operated by the same entity and a farmworker who picks produce at two separate orchards, where the orchards have arranged to share farmworkers. The hallmark of this arrangement is some type of cooperation or administrative coordination among the separate employers. The FLSA regulations governing joint employment, which also focus on the relationship of the employers to each other, are instructive here, whether the case arises under the MSPA or the FLSA.

In analyzing the relationship between potential horizontal joint employers, the FLSA regulations look for arrangements between the employers to share or interchange the employee's services, or where one employer acts (directly or indirectly) in the interests of another employer in relation to the employee, or where the employers share control of the employee (directly or indirectly) because one employer controls, is controlled by, or under common control with the other employer. In the AI, however, the DOL suggests a number of non-exhaustive factors to be considered, the focus of which is on the relationship (and often the degree of association) between the two (or more) potential joint employers, including the following:

- Who owns the potential joint employers (i.e., does one employer own part or all of the other or do they have any common owners);
- Whether the potential joint employers have any overlapping officers, directors, executives, or managers;

- Whether the potential joint employers share control over operations (e.g., hiring, firing, payroll, advertising, overhead costs);
- Whether the potential joint employers' operations are inter-mingled (for example, is there one administrative operation for both employers, or does the same person schedule and pay the employees regardless of which employer they work for);
- Whether one potential joint employer supervises the work of the other;
- Whether the potential joint employers share supervisory authority for the employee;
- Whether the potential joint employers treat the employees as a pool of employees available to both of them;
- Whether the potential joint employers share clients or customers; and,
- Whether there are any agreements between the potential joint employers.

Not all of the above facts need to be present for joint employment to exist. The DOL distinguishes horizontal joint employers from employers that "are acting entirely independently of each other and are completely disassociated with respect to an employee who works for both of them."[5] In the latter case, joint employment does not exist. By way of example, the DOL explains that a high school teacher who also worked as a tutor for a standardized test preparatory company would not be considered jointly employed by both the high school and the test prep company, as long as there was no relationship or intermingled operations between the two companies.

In sum, the central focus of a horizontal joint employment analysis is the relationship between the employers and the amount of control they share with respect to the employee.

Vertical Joint Employment

In contrast to the horizontal joint employment inquiry's focus on the relationship between the employers, the focus in a vertical joint employment analysis is the employee's relationship with the potential joint employer. According to the DOL, vertical joint employment relationships typically arise where the potential joint employer has contracted or made arrangements with the intermediary employer to provide it with labor and/or certain business functions, such as hiring or payroll. Although there is usually an established employment relationship between the employee and the intermediary employer, the employee's work typically benefits the potential joint employer as well. A prime example of a potential vertical joint employment scenario is an individual who is assigned by a staffing agency to work at a separate company. The AI cites the MSPA regulations as "useful guidance" in analyzing any vertical joint employment case.

The vertical joint employment analysis consists of two parts. Under the initial part of the analysis, the DOL determines whether the intermediary employer is actually an employee of the potential joint employer. If the answer is yes, then the intermediary employer's employees are employees of the potential joint employer as well and the inquiry ends there. While it may seem that only an individual could be deemed to be an employee of the potential joint employer, in fact, under the DOL's view, entities can also be deemed to be "employees." For this proposition, the DOL cites a prior Administrator's Interpretation, No. 2015-1[6], which was previously discussed in the Autumn 2015 edition of *Insights*, (available at http://www.slk-law.com/NewsEvents/Publications/123508/Your-Drivers-Are-Now-Your-Employees-Independent-Contractors-Under-the-New-Labor-Paradigm). There, the DOL addressed the proper classification of workers as either independent contractors or employees, and, largely relying on the same economic realities test, determined that most workers are properly classified as employees.

The DOL also provides several examples of vertical joint employment under this standard, including a farm labor contractor who is employed by a grower, but also employs his own farmworkers and a subcontractor who is employed by a general contractor, but also employs his own workers. Under these examples, both the farm laborer's employees and the subcontractor's employees are all employees of the potential joint employers, the grower and the general contractor. In addition, the DOL disregards the corporate form in making this determination.

If the intermediary employer is not an actual employee of the potential joint employer, the DOL requires that the vertical joint employment inquiry proceed to its second step – the "economic realities" analysis.

The AI specifically mandates that the vertical joint employment analysis **cannot** focus only on control, which is a stark departure from the control-centered analysis previously (and in some cases currently) applied by the courts. Instead, the central question is "whether the employee is economically dependent on the potential joint employer who, via an arrangement with the intermediary employer, is benefitting from the work."[7]

To answer that central question, the DOL looks to the seven economic realities factors described in the MSPA's joint employment regulation, 29 C.F.R. § 500.20(h)(f)(iv), but notes that the economic realities factors "should not be considered mechanically or in a vacuum; rather they are guides for resolving the ultimate inquiry whether the employee is economically dependent on the potential joint employer."[8] These factors include the following:

- Whether and to what extent the potential joint employer controls or supervises, either directly or indirectly, beyond a reasonable degree of contract performance oversight, the work performed by the employee;
- Whether and to what extent the potential joint employer has the power, directly or indirectly, to hire or fire the employee, modify employment conditions, or determine the rate or method of pay;
- The degree of permanency and duration of the relationship, considered in the context of the particular industry at issue;
- The extent to which the services rendered by the employee are repetitive, rote tasks requiring skills that are acquired with relatively little training;
- Whether the activities performed by the employee are an integral part of the overall business operation of the potential joint employer's business;
- Whether the work is performed on the potential joint employer's premises; and,
- Whether the potential joint employer performs administrative functions for the employee, such as handling payroll, providing workers' compensation insurance, providing necessary facilities and safety equipment, housing or transportation, or providing tools and equipment or materials required for the job.

Recognizing that the economic realities factors may vary by court, the DOL requires that every formulation "address the ultimate inquiry of economic dependence" and recognize "the broad scope of joint employment under the FLSA and MSPA."[9] Consequently, the DOL expressly rejected the approach applied by some courts which primarily or exclusively focuses on the potential joint employer's control, specifically hiring and firing authority, supervision and control of employment conditions or work schedules, determination of rates and methods of pay, and maintenance of employment records. This approach, the DOL concludes, "is not consistent with the breadth of employment under the FLSA."

In sum, any vertical joint employment analysis must consider the broad scope of employment under the FLSA and MSPA and resolve the ultimate inquiry of whether the employee is economically dependent on the potential joint employer.

How Does the AI Impact Employers?

The AI very clearly demonstrates that the DOL intends to interpret the FLSA as broadly as possible to protect employees and ensure that employers cannot evade their obligations under the statute by sharing employees with related entities or utilizing staffing agencies or contractors for labor. While the DOL does not significantly alter the horizontal joint employment analysis, its rejection of the common law control-based formulations in favor of the broader economic realities for the vertical joint employment analysis will likely have significant implications for employers that contract with third parties for staffing and administrative functions, or that share employees with affiliated entities.

For instance, as the DOL notes, when two or more employers jointly employ an employee, the employee's hours worked for **each joint employer** during each workweek are aggregated and considered as one employment for purposes of calculating minimum wage and overtime. Thus, employers that qualify as joint employers under the FLSA will need to implement procedures to record **all** hours worked by each employee of all of its joint employers, in order to calculate minimum wage and overtime based on the sum of all the hours worked in a workweek. Suppose, for example, that Companies A, B, and C jointly employ Mr. Smith and, during a particular workweek, Mr. Smith works 10 hours for Company A, 30 hours for Company B, and 20 hours for Company C. Under the FLSA's joint employer provisions, Mr. Smith would have worked a 60 hour workweek and would be entitled to overtime

for 20 of those hours. The three companies are responsible for paying the 20 hours of overtime, although the companies need not pay 20 hours of overtime each. How such overtime payments will be paid by the three companies must be determined as a matter of negotiation among the three companies.

Making matters worse, joint employers are jointly and severally liable for FLSA violations, including minimum wage and overtime violations. The DOL explains that "[i]f one employer cannot pay the wages because of bankruptcy or other reasons, then the other employer must pay the entire amount of wages; the law does not assign a proportional amount to each employer."[10] Thus, if the aforementioned Companies A and B cannot pay Mr. Smith's wages for that workweek, Company C must compensate Mr. Smith for all 60 hours worked, including the 20 hours of overtime, or face full liability for its failure to ensure the overtime is paid.

Moreover, should the DOL's analysis in the AI begin to permeate other employment law contexts, such as liability for employing unauthorized workers or for discriminatory acts, a joint employer could find itself liable for a host of violations committed by subcontractors, staffing agencies, and affiliated entities.

Given the severe consequences that employers face for violating the FLSA – specifically, back wages, liquidated damages, and attorneys' fees of both the employer and the employee(s) – we strongly recommend that all employers that currently share employees with related entities or contract with third party providers for labor or administrative services assess their employment relationships by reviewing the factors identified in the AI and confirm whether or not they qualify as a joint employer under either the horizontal or vertical joint employment analyses.

In light of the high risk of liability, employers who believe they may qualify as a joint employer should review their business models to determine whether the sharing of employees and/or the use of employees provided by third parties can be eliminated. If the employer's business model is reliant upon shared employees and/or contracted workers, we recommend that the employer review and amend their written agreements with its potential joint employers to establish each party's obligations with respect to employment law compliance, particularly FLSA compliance, and include specific provisions allocating responsibility for overtime payments and other compliance, as well as strong indemnification provisions in favor of the contracting employer as an additional safeguard.

Shumaker's experienced Labor and Employment attorneys stand ready to assist you with undertaking the recommended analysis, as well as any required contract review or drafting to ensure compliance with the DOL's latest trend toward expanding the definition of employment in all its forms. You can contact the authors, Kate Decker (kdecker@slk-law.com) and Mechelle Zarou (mzarou@slk-law.com), or any member of Shumaker's Labor and Employment Department for immediate assistance.

[1] AI at 4, quoting *Antenor v. D & S Farms*, 88 F.3d 925, 933 n. 10 (11th Cir. 1996) (internal quotation marks omitted).

[2] AI at 2-3.

[3] *Id.* at 3.

[4] *Id.* at 2-3.

[5] AI at 9, quoting 29 C.F.R. § 791.2(a) (internal quotation marks omitted).

[6] Administrators Interpretation No. 2015-1 (hereinafter "Misclassification AI").

[7] AI at 11.

[8] AI at 11, citing *Antenor*, 88 F.3d at 923-33 and the Misclassification AI, 5-6.

[9] AI at 13 (internal quotation marks omitted).

[10] AI at 2, fn. 4.