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Labor & Employment ADVISORY ■

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New Department of Labor Guidance Continues Assault on Definition of Joint Employer

The Wage & Hour Division (WHD) of the U.S. Department of Labor (DOL) issued new guidance in January that could substantially impact the business models and potential liabilities for any employer that regularly contracts with third parties for outsourcing or staffing. On January 20, 2016, the DOL published Administrator's Interpretation No. 2016-1 (the "AI"), which calls for increased scrutiny of certain business models and labor arrangements and seeks to expand the definition of "employer" under the Fair Labor Standards Act (FLSA) through a liberal interpretation of when two or more businesses may be considered "joint employers" under the FLSA. As a consequence, companies that contract with other businesses now face even more potential liability when a subcontractor fails to comply with the FLSA.

The AI follows on the heels of another guidance letter issued by the DOL in July 2015, in which the DOL likewise sought to expand the definition of "employee" under the FLSA by taking the position that "most workers" qualify as employees, not independent contractors, under the FLSA's "economic realities test." Similarly, in a third significant move by a federal government agency, the National Labor Relations Board (NLRB) overruled longstanding precedent in its August 2015 *Browning-Ferris* decision to find that a contractor's "indirect control" of a subcontractor's workers may cause it to be considered a joint employer under the National Labor Relations Act (NLRA) even when the contractor has not demonstrated any overt control over the terms and conditions of the subcontractor's workers' employment. Overall, these three regulatory interpretations reflect a general trend under the current administration to expand federal laws such that "bigger fish" employers can be held liable for back wages, penalties and a host of other damages that smaller subcontractors may have been exclusively liable for under prior interpretations. As stated in the AI:

> Where joint employment exists, one employer may also be larger and more established, with a greater ability to implement policy or systemic changes to ensure compliance. Thus, WHD may consider joint employment to achieve statutory coverage, financial recovery, and future compliance, and to hold all responsible parties accountable for their legal obligations.

In the AI, the DOL asserts the scope of joint employment should be construed "as broad as possible" via the FLSA's

"economic realities" test.[1] Under that test, a business is to be held responsible for work performed by a third party's employee if the worker in question is "economically dependent on, and thus employed by" the contracting entity in addition to the employee's direct, subcontracted employer.

The AI then further differentiates between two different types of joint employment relationships. Specifically, "horizontal" joint employment may arise when, for example, a single employee works for two separate and independent businesses, but both are jointly owned and/or operated by a single business entity. According to the DOL, in that situation both businesses, as well as the parent company, can each be held jointly and severally liable for any wages due to the employee by any of the three. Clearly, this interpretation could impact any situation where contractors are used to staff or provide services to otherwise independent, discrete subsidiaries operating under a common parent.

In applying the "horizontal joint employer" test under the new written guidelines, the DOL will look to whether two separate employers are sufficiently related to be considered joint employers. Specifically, the DOL will consider:

- Who owns the potential joint employers.
- Whether the potential joint employers have any overlapping officers, directors, executives or managers.
- Whether the potential joint employers share control over operations like hiring, firing, payroll, advertising and overhead costs.
- Whether the potential joint employers' operations are or have been intermingled.
- Whether one potential joint employer supervises the work of the other.
- Whether the potential joint employers share supervisory authority for the employee in question.
- Whether the potential joint employers treat the employees as a pool of employees available to them both.
- Whether the potential joint employers share clients or customers.
- Whether there are any agreements between the potential joint employers.

The AI's position on "vertical" joint employment, by contrast, may significantly impact employers that utilize third-party staffing services in their business models or outsource business functions to a third-party employer. This arises when an employee has an employment relationship with one employer, but the employee is "economically dependent" upon another entity that can therefore be considered a joint employer for purposes of the FLSA. According to the DOL, this analysis "is used to determine, for example, whether a construction worker who works for a subcontractor is also employed by the general contractor, or whether a farmworker who works for a farm labor contractor is also employed by the grower." Under this test, the DOL will closely examine the nature of the contracted work to determine whether joint employment status exists by considering:

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[1] Notably, in *Browning-Ferris* the NLRB expressly asserted that it was stopping short of applying the FLSA's "economic realities" test in that case – a test that the U.S. Supreme Court has described as embodying the broadest definition of "employment" of any employment law in the country. *See U.S. v. Rosenwasser*, 323 U.S. 360, 363 n.3 (1945). Nonetheless, both the NLRB's decision and the DOL's most recent AI adopt the view that a business does not have to *directly control* a worker's employment to be responsible for regulatory compliance with laws governing that worker's employment conditions, a requirement that has traditionally formed the backbone of joint employer analysis under the common law.

- The extent work performed by the employee in question is controlled or supervised by the potential joint employer beyond a reasonable degree of contract performance oversight.[2]
- The extent the potential joint employer has the power to hire or fire the employee, modify employment conditions or determine the rate or method of pay.
- The permanence and duration of the business relationship.
- How repetitive, rote or unskilled the employee's work that he or she does for the potential joint employer is and how much training it requires.
- The extent the employee's work constitutes an integral part of the potential joint employer's business.
- The extent the employee performs his/her work on premises owned or controlled by the potential joint employer.
- The extent 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 materials required for the work.

Because businesses that are joint employers can be held jointly and severally liable for minimum wage, overtime and other obligations under the FLSA, the DOL's new guidelines could have enormous implications for businesses that contract for staffing or outsourcing purposes (e.g., the staffing, hospitality, construction, janitorial, agricultural, warehouse and logistics industries were all specifically referenced in the AI). This is particularly true in light of the increased DOL investigative activity that employers have been facing in recent years. While the AI is not binding "law," such regulatory guidance is generally viewed as persuasive authority by the courts, which may therefore become increasingly reluctant to dismiss FLSA claims against contracting employers early on based on an assertion that the contractor was not the "employer" of the allegedly underpaid employees.

Regardless of whether the DOL's opinions are ultimately adopted by courts, however, there is little doubt that the DOL will seek to enforce its new position in its investigations and in litigation. There is also little doubt that the plaintiffs' bar will waste no time in seeking out potential class representatives to file wage claims against general contractors as joint employers based on even the most tenuous of business relationships. Therefore, large employers, general contractors, franchisors, staffing agencies and even private equity firms should all expect to see an uptick in the number of federal wage-and-hour lawsuits being filed against them in the near future.

Accordingly, employers that use staffing services or outsource functions to third parties should consider several steps to mitigate their risk. First, contracting employers may wish to re-evaluate their business models and consider alternate arrangements, particularly where the employers rely heavily on temporary employees or independent contractors to supplement their regular work forces and where employers outsource core administrative or operational functions to third parties. In such cases, it may be advisable to reduce the employer's reliance on non-employee workers and bring more work back in-house. Second, contracting employers should examine their written agreements with staffing companies and outsourcing partners and, if possible, take steps to revise those agreements to further confirm the "separateness" of the two employers. Indemnification provisions should also be revised to better protect

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[2] According to the AI, the potential joint employer's control can be indirect (for example, exercised through the intermediary employer) and still be sufficient to indicate economic dependence by the employee. Thus, according to the DOL, the potential joint employer need not exercise more control than, or even the same control as, the intermediary employer in order to exercise sufficient control to indicate the economic dependence of the employee.

the contracting employer in case an employee of a third-party employer sues both entities under a joint employer theory. Third, contracting employers should review and, if necessary, revise their practices to minimize the degree of day-to-day supervision and control over the workers who are assigned by the staffing agency or employed by outsourcing partners. Finally, given the potential for increasing joint employer scrutiny and potential liability in the future, it may be advisable for contracting employers to better vet potential business partners to ensure that they have solid employment policies and practices in place and do not have a record of wage and hour violations.

For all of these reasons, then, any employers that regularly outsource work or employ subcontractors for staffing or other services should take notice of the AI, keep close tabs on its development in the courts and adjust their business strategies accordingly. Alston & Bird would be happy to assist clients who feel that they may be impacted by the new DOL guidance in assessing and re-evaluating their existing contractor relationships, and to help better position their business models and third-party relationships to avoid potential enforcement actions and litigation in the future.

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