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Practical Strategies for Mitigating FLSA Joint Employment Risk in Light of Recent 4th Circuit Decisions

Businesses in a variety of industries routinely rely upon the labor of third-party contractors and vendors to provide services. These arrangements promote efficiency and flexibility by allowing companies to pay for certain services on an "as-needed" or project-by-project basis. However, the increased use of these arrangements also comes with increased risks—a company can be deemed a "joint employer" of its contractors' workers and face significant liability under the Fair Labor Standards Act (FLSA) and other employment laws.

Joint employment was a prominent issue for the U.S. Department of Labor (DOL) during the Obama administration. The DOL's focus on the issue culminated in extensive informal guidance that took an expansive, pro-employee view of joint employment. This guidance was withdrawn in June.[1] However, area companies should not be lulled into a false sense of security on this issue because, this year, the 4th Circuit Court of Appeals created a standard that arguably has lowered the bar for plaintiffs in Virginia and Maryland to establish joint employment under the FLSA.

The 4th Circuit's approach minimizes the impact of the DOL's policy reversal and endorses an expansive view of joint employment under the FLSA and equivalent state laws regardless of what nonbinding guidance is issued by the DOL, a view that could be adopted by other jurisdictions. Given this new test and the 4th Circuit's stated intent to "broadly" interpret the FLSA to effectuate its "remedial and humanitarian purpose," area companies should reassess their third-party contractor relationships and take proactive steps to mitigate joint employment risks.

Joint Employment Under the FLSA

The FLSA applies only to "employees," not independent contractors. Thus, if a worker is an "employee" and is not otherwise exempt, he or she is entitled to overtime pay for all hours more than 40 worked in a week. Under the FLSA, "employee" is defined broadly as "any individual employed by an employer."[2] Similarly, "employer" is expansively defined as "any person acting directly or indirectly in the interest of an employer in relation to an employee."[3] Although the FLSA does not expressly define "joint employment," the DOL's

[1] *See* News Release, *US Secretary of Labor Withdraws Joint Employment, Independent Contractor Informal Guidance* (June 7, 2017), *available at* https://www.dol.gov/newsroom/releases/opa/opa20170607.

[2] 29 U.S.C. § 203(e)(1).

[3] *Id.* at § 203(d).

regulations state that "joint employment" exists when the "facts establish . . . that employment by one employer is not completely disassociated from employment by the other employer(s) . . . ."[4]

The DOL's regulations set forth three situations where joint employment exists:

- where there is an arrangement between the employers to share the employee's services, as, for example, to interchange employees
- where one employer is acting directly or indirectly in the interest of the other employer (or employers) in relation to the employee or
- where the employers are not completely disassociated with respect to employment of a particular employee and may be deemed to share control of the employee, directly or indirectly, by reason of the fact that one employer controls, is controlled by or is under common control with the other employer.[5]

Companies found to be joint employers are treated as a single employer for the purposes of determining compliance with the FLSA and are jointly and severally liable for violations.

Courts have adopted various tests for determining whether two companies are joint employers. In *Bonnette v. California Health and Welfare Agency*,[6] the 9th Circuit announced one of the first such tests. Under *Bonnette*, a court assesses whether the alleged employer exercised control over the terms and conditions of the plaintiff's employment because it (1) had the power to hire and fire the employees, (2) supervised and controlled employee work schedules or conditions of employment, (3) determined the rate and method of payment, and (4) maintained employment records. Several other circuits have adopted variations of the *Bonnette* factors.[7] Many of these tests consider not only the control that the alleged employer exercised over the worker, but also the "economic dependence" of the worker on the alleged employer. In all of these tests, courts focus on the relationship between the alleged employer and the worker.

Prior to this year, the 4th Circuit had not adopted express factors for analyzing alleged joint employment, causing federal district courts in the 4th Circuit to apply a variety of multifactor tests derived from other circuits.[8]

The 4th Circuit's Test

[4] 29 C.F.R. § 791.2(a).

[5] *Id.* at § 791.2(b).

[6] 704 F.2d 1465 (9th Cir. 1983).

[7] *See Baystate Alternative Staffing, Inc. v. Herman*, 163 F.3d 668 (1st Cir. 1998); *Zheng v. Liberty Apparel Co.*, 355 F.3d 61 (2d Cir. 2003); *In re Enter. Rent-A-Car Wage & Hour Emp't Practices Litig.*, 683 F.3d 462 (3d Cir. 2012); *Orozo v. Plackis*, 757 F.3d 445 (5th Cir. 2014); *Layton v. DHL Express (USA), Inc.*, 686 F.3d 1172 (11th Cir. 2012).

[8] *See, e.g.*, *Dalton v. Omnicare, Inc.*, 138 F. Supp. 3d 709 (N.D. W. Va. 2015) (applying four-factor *Bonnette* test); *Jennings v. Rapid Response Delivery, Inc.*, No. WDQ-11-0092, 2011 WL 2470483 (D. Md. June 16, 2011) (applying nine-factor test derived from *Bonnette* and *Zheng*).

On January 25, 2017, the 4th Circuit issued its decision in *Salinas v. Commercial Interiors Inc.*, 848 F.3d 125 (4th Cir. 2017), setting forth a new joint employment test.[9] In *Salinas*, the plaintiffs were employees of J.I. General Contractors ("J.I."), a company that worked almost exclusively as a subcontractor for Commercial Interiors, Inc. ("Commercial") providing drywall installation. Commercial offered general contracting and interior finishing services, including drywall installation, carpentry, framing and hardware installation. The plaintiffs sued both companies, alleging that they jointly employed the plaintiffs and were liable for unpaid overtime under the FLSA and Maryland law. The district court found that the defendants were not joint employers because they had entered a legitimate and "traditionally . . . recognized" subcontracting relationship and did not intend to evade federal or state law.

On appeal, the 4th Circuit reversed. In doing so, it held that the *Bonnette* factors (1) improperly focus on the relationship between the employee and the alleged employer, rather than on the relationship between the putative joint employers, and (2) incorrectly frame the joint employment inquiry as a question of an employee's "economic dependence" on the alleged joint employer.

The 4th Circuit uses a two-step framework in FLSA cases where the plaintiff's status as an employee of an alleged joint employer is in dispute. First, the court considers whether the companies involved are joint employers. Then, if they are, the court analyzes whether the worker is an employee or independent contractor of the **combined** entity. In *Salinas*, the 4th Circuit announced six nonexclusive factors to consider at step one:

- whether, formally or as a matter of practice, the putative joint employers jointly determine, share or allocate the power to direct, control or supervise the worker, whether by direct or indirect means
- whether, formally or as a matter of practice, the putative joint employers jointly determine, share or allocate the power to—directly or indirectly—hire or fire the worker or modify the terms or conditions of the worker's employment
- the degree of permanency and duration of the relationship between the putative joint employers
- whether, through shared management or a direct or indirect ownership interest, one putative joint employer controls, is controlled by or is under common control with the other putative joint employer
- whether the work is performed on a premises owned or controlled by one or more of the putative joint employers, independently or in connection with one another
- whether, formally or as a matter of practice, the putative joint employers jointly determine, share or allocate responsibility over functions ordinarily carried out by an employer, such as handling payroll; providing workers' compensation insurance; paying payroll taxes; or providing the facilities, equipment, tools or materials necessary to complete the work.

[9]On that same day, the 4th Circuit issued another collective action wage and hour decision applying the *Salinas* joint employment test. *See Hall v. DIRECTV, LLC*, 846 F.3d 757 (4th Cir. 2017).

Applying this test, the 4th Circuit found that J.I. and Commercial were not "completely disassociated" and were thus joint employers. The court relied on the following facts:

- J.I. performed nearly all of its work for Commercial on Commercial jobsites.
- Commercial provided tools, materials and equipment necessary for the plaintiffs' work.
- Commercial provided lodging for J.I. employees on at least one occasion.
- Commercial actively supervised the plaintiffs' work on a daily basis by having foremen walk the jobsite and check their progress.
- Commercial required the plaintiffs to attend frequent meetings regarding their tasks and safety protocols.
- Commercial required the plaintiffs to sign in and out with Commercial foremen when they reported to and left the jobsite each day.
- Commercial communicated problems with the plaintiffs' work to J.I. supervisors who translated the information to Spanish.
- Commercial foremen told certain plaintiffs to work additional hours or days.
- J.I. based the plaintiffs' job assignments on Commercial's needs.
- When J.I. was paid based on an hourly rather than lump-sum basis, Commercial told J.I. how many employees to send to the project and capped their hours worked.
- Commercial provided the plaintiffs with Commercial-branded clothing.
- J.I. instructed the plaintiffs to tell anyone who asked that they worked for Commercial.
- On at least one occasion, Commercial required J.I. employees to apply for employment with Commercial and directly hired those employees.

Having concluded that J.I. and Commercial were joint employers, the court next analyzed whether, "based on their 'one employment' with Commercial and J.I.," the plaintiffs were "employees" within the meaning of the FLSA or independent contractors. At this step, the court applied a multifactor "economic realities" test in holding that Commercial jointly employed the plaintiffs for purposes of the FLSA.[10]

Implications of the 4th Circuit's Test

[10] In the 4th Circuit, the factors are (1) the degree of control that the putative employer has over the manner in which the work is performed; (2) the worker's opportunities for profit or loss dependent on his or her managerial skill; (3) the worker's investment in equipment or material, or his or her employment of other workers; (4) the degree of skill required for the work; (5) the permanence of the working relationship; and (6) the degree to which the services rendered are an integral part of the putative employer's business.

The 4th Circuit's new test may make it more difficult to defend joint employment claims. Indeed, some of the facts the 4th Circuit relied upon to find joint employment are common to the contractor and subcontractor relationship. For example, the court held that Commercial's feedback and instruction to J.I. supervisors about the plaintiffs' work and requirement that J.I.'s workers attend meetings about the project and safety protocols amounted to "extensive supervision indicative of an employment relationship." In the court's view, whether Commercial's relationship with J.I. was "normal and standard in the construction industry" was irrelevant to determining joint employment status under the FLSA.

While *Salinas* directly impacts claims related to employers operating in states covered by the 4th Circuit (Maryland, North Carolina, South Carolina, Virginia, and West Virginia), courts outside the 4th Circuit and administrative agencies may adopt the 4th Circuit's approach. For example, in May, a district judge in Colorado, deciding a putative employer's motion for summary judgment, wrote that, "[i]f the Court were writing on a clean slate, it would likely . . . be persuaded to adopt the test recently pronounced by the Fourth Circuit . . . in [*Salinas*]."[11] The court declined to adopt the 4th Circuit's test only because it was announced after the defendant's motion had been filed.

Furthermore, some courts have already been moving away from the control factors in *Bonnette* to look at a variety of other factors. For example, in *Zheng v. Liberty Apparel Co.*, the 2nd Circuit held that addressing only the putative joint employer's control of the worker was an "unduly narrow" approach that could not "be reconciled with the 'suffer or permit' language in the [FLSA], which necessarily reaches beyond traditional agency law." With the *Salinas* test creating additional momentum, this movement toward a more expansive view of joint employment may accelerate.

Practical Actions to Mitigate the Risk of Joint Employment

Area companies should assess their relationships with third-party contractors in light of *Salinas*. When assessing those relationships, companies should consider the following practices:

- **Insourcing:** Consider whether it makes sense to outsource the work to a third-party contractor in the first place. Outsourcing work that is longterm, requires a highlevel of control over the contractor, or arguably involves the core services or products offered by the company will increase the risk of joint employment.

- **Vet Third-Party Contractors for Compliance with Employment Laws:** Before engaging a third-party contractor, conduct diligence on the contractor's employment practices, including requiring the contractor to provide information on its wage and hour compliance, practices for classifying workers, payment methods, recordkeeping, and wage and hour claims. Equally important is ensuring that the contractor maintains its own employment policies and records.

- **Execute Good Independent Contractor Agreements:** Having—and abiding by—good agreements with third-party contractors will strengthen defenses against joint employment claims. Specifically, the agreement should identify the contractor as an "independent

[11] *See Sanchez v. Simply Right, Inc.*, No. 15-cv-00974-RM-MEH, 2017 WL 2222601, at *7 n.13 (D. Colo. May 22, 2017).

contractor" and state that the contractor is responsible for all terms and conditions of its employees' employment, including wages and benefits, hiring and supervision. The agreement should also expressly limit the company's ability to exercise control over the contractor's employees, including supervision, discipline, hiring or firing. Having strong indemnification language can also help ensure that the company has a remedy for fees, expenses and monetary damages related to joint employment claims, although such indemnification provisions may not be a direct defense to the employee's claims.

- **Do Not Provide Equipment, Tools or Uniforms:** Contractors should supply all tools and equipment for their workers to provide services under the contract. Avoid having a contractor's workers wear company uniforms or anything else that may give the impression that they are company employees.

- **Avoid Scheduling or Assigning Tasks:** Avoid scheduling a contractor's workers or assigning them tasks. To the extent that the contractor needs to perform work or tasks at certain times, make clear that the contractor has absolute control over which workers perform the tasks and the details of how the job is completed. The contractor can still engage in quality control focused on deliverables and outcomes, not the manner in which the job is performed. To the extent that government regulations require the company to ensure that certain safety or other standards are met, the restrictions and training given to contractors should focus on the regulatory requirements and not additional standards imposed by the company.

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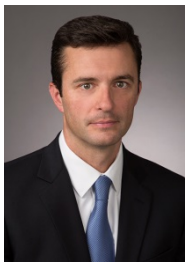

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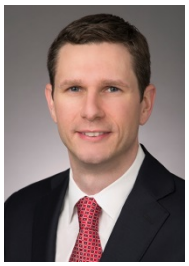

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