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W A G E A N D H O U R

Joint Employer Liability Under the Wage-and-Hour Laws

BY ANDREA M. KIRSHENBAUM

Special to the Legal

When the National Labor Relations Board's (NLRB) Office of General Counsel announced in August that it was authorizing complaints against both McDonald's store owners and corporate McDonald's USA LLC as so-called "joint employers," the employer community was abuzz, fearing wide-reaching application of the National Labor Relations Act (NLRA) to corporate entities, or franchisors, that were removed from the day-to-day operation of the business. While there has not been a similar singular moment in the wage-and-hour arena, over the last several years workers have attempted to expand the concepts of "employer" and "employee" under the Fair Labor Standards Act (FLSA) and state wage-and-hour law in an effort to obtain additional potential reservoirs of recovery.

While the decision of the NLRB's general counsel relates to application of the NLRA and does not directly impact how the FLSA, a separate statute, is or will be interpreted, it is emblematic of a growing trend to expand the definitions of employer and employee under a variety of labor and employment laws. Just one example is the U.S. Court of Appeals for the Seventh Circuit's decision just last month finding that Trans States Airlines and GoJet Airlines, two air carriers that provided air services to United Airlines at Chicago O'Hare International Airport,



ANDREA M. KIRSHENBAUM

is a principal in the Philadelphia office of Post & Schell and is part of the firm's employment and employee relations law practice group. She litigates and provides compliance counseling on wage-and-hour issues for employers. She can be contacted at akirshenbaum@postschell.com.

were joint employers under the Family and Medical Leave Act of 1993.

That the definition of an employer is a hotly litigated topic in wage-and-hour law is not surprising. The FLSA allows for employees to be employed by multiple entities, and individuals simultaneously, and as a result, presents a greater number of potential companies and individuals that can be named in a wage-and-hour lawsuit. Plaintiffs, seeking to increase the likelihood that they will have someone to recover damages from should they succeed in the litigation, are increasingly naming several entities—including parent entities, franchisors and individuals—as parties to wage-and-hour litigation.

Employers should take heed of efforts to expand the universe of "employers" and "employees" under the wage-and-hour laws, and take the necessary steps to mitigate against the risk created by such claims.

EXPANDING THE DEFINITION OF EMPLOYER

The FLSA defines an "employer" as "any

person acting directly or indirectly in the interest of an employer in relation to an employee" and "employee" as "any individual employed by an employer." The U.S. Supreme Court has stated that the FLSA's definition of employer is "the broadest definition that has ever been included in any one act."

Some wage-and-hour attorneys in the plaintiffs bar have seized upon these definitions of employer and employee, arguing that individuals ostensibly are employed by everyone, the kitchen sink and more. Often relying upon the less onerous notice pleading requirements in federal court, as opposed to the more arduous obligations to plead facts in many states, plaintiffs are increasingly naming the so-called "big fish," as well as many other medium and small fish. The reasons for doing so are varied. Plaintiffs often seek to name the parent entity, franchisor or entity that subcontracts for their direct employer's services to create a larger potential class size and hence a larger potential pool of recovery. Also, by naming the so-called deep-pocket, plaintiffs attempt to reduce the chances of being faced with a judgment-proof defendant. While the naming of individual employees certainly does not serve that same objective, it often creates significant institutional discomfort as senior-level employees understandably are troubled by being a party in litigation due to decisions made within the scope of their employment.

This trend should give parent companies, franchisors and companies that subcontract

services significant pause. As many franchisors have begun to take stock of their practices in the wake of the NLRB's Office of General Counsel announcement that it is naming corporate McDonald's as a joint employer in unfair labor practice proceedings, so too employers should assess their risks in the wage-and-hour joint employer arena.

EXPANDING THE DEFINITION OF EMPLOYEE

At the same time that employees are working to expand the definition of employer, enterprising plaintiffs attorneys also are taking aim at the traditional notions of employment, specifically who qualifies as an employee under the wage-and-hour laws. In the franchise context, plaintiffs in several cases have taken the position under various state laws that franchise owners are entitled to the protections of the wage-and-hour laws as employees, because, the argument goes, they are tightly controlled by franchisors such that they qualify as employees. In one such case brought against cleaning company franchisor Jani-King of California Inc., a district court in California rejected this argument on summary judgment and found franchisees to be independent contractors.

The question of who qualifies as an "employee" as opposed to an employer or part-owner in an entity also can be an issue in startup companies, which often are strapped for cash in their infancy. Startup owners sometimes choose to forgo paying themselves a salary in lieu of (hopefully growing) equity in the nascent enterprise. This, of course, can create wage-and-hour risk should the part-owners be found to qualify as employees under the wage-and-hour laws, and therefore entitled to minimum wage and overtime.

OUTSOURCING AND JOINT EMPLOYMENT

In the age of outsourcing certain projects or functions (consultants, IT help desk, cleaning services, etc.) and using temporary workers, the expansion of wage-and-hour litigation can hit companies, as well as

individuals, in multiple and varied ways. Yet, if defendants in wage-and-hour litigation are not the "employers" of the workers in the traditional sense (do not track hours, provide paychecks, etc.), they can find themselves in an untenable position in litigation, lacking the information they need to mount an effective defense on the merits of the case.

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Thankfully, employers are not without tools in their arsenal to reduce their exposure to wage-and-hour litigation (or to allocate the responsibility for litigation in advance).

The Third Circuit has applied the following non-exhaustive four-factor test to analyze whether an entity or individual qualifies as a joint employer under the FLSA. The test looks to whether the alleged employer has: (1) authority to hire and fire employees; (2) authority to promulgate work rules and assignments, and set conditions of employment, including compensation, benefits and hours; (3) day-to-day supervision, including employee discipline; and (4) control of employee records, including payroll, insurance, taxes and the like.

These guideposts are useful tools for entities to assess their relationship with workers and subcontractors, and to avoid any indicia of functional control over the employees of contractors, franchisees or subsidiary entities. In the subcontracting context, companies must to the maximum extent feasible allow the contracting agency to supervise and set the terms and conditions under which the

contractor's employees perform their duties. While this may be easier said than done, it is essential for organizations to continuously evaluate the extent to which their managers are exercising any supervisory authority over a contractor's employees. And certainly, companies can negotiate robust defense and indemnification provisions with subcontractors as well as require subcontractors to carry adequate insurance and name the companies as additional insureds on their insurance policies to allocate responsibility for potential wage-and-hour litigation ex ante should it rear its ugly head.

Insurance also can serve to reduce the risk of wage-and-hour litigation. While traditionally wage-and-hour coverage has been difficult to obtain (and wage-and-hour litigation often is an exclusion in standard employment practices liability insurance coverage), it is becoming increasingly available. While the deductible can be higher than traditional employment practices liability insurance policies, insurance coverage can serve as a stopgap to prevent wage-and-hour litigation from forcing a small business to close its doors.

As the traditional employer-employee relationship erodes in favor of various other types of relationships that are less easily classified, workers will continue to challenge the contours of what it means to be an "employer" or an "employee" under wage-and-hour laws. Faced with the current legal landscape, employers should assess their vulnerabilities to "joint employer" challenges and work to put in place effective strategies to address this legal risk. •