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ALERT

SDNY Court Knocks Down DOL's Joint-Employer Rule

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WHAT: On September 8, 2020, a Judge for the Southern District of New York (SDNY) in Manhattan declared key portions of the Department of Labor's (DOL) recent joint-employer rule illegal, essentially gutting the rule which was widely lauded by employers. The rule, which took effect in March, narrowed the scenarios in which multiple employers could be held liable under the Fair Labor Standards Act (FLSA) for the same employee. The SDNY struck the portion of the rule that applied to "vertical" employment relationships, for example when employees of a subcontractor are contracted to work for another company, finding that this portion of the rule was "arbitrary and capricious" and inconsistent with the FLSA.

BACKGROUND: Under the FLSA, when more than one employer "suffers or permits" the same individual to work, both employers may be held jointly and severally liable for wage and hour violations based on the nature of control each employer has over that individual employee's work. This is the joint-employer relationship. Whether or not both employers are in fact joint employers has historically been a muddy area of law, with courts and agencies applying varied tests as administrations changed, creating uncertainty for employers.

Partially in response to this unpredictability, the DOL published a new rule regarding joint employers in January 2020. This rule created a four-factor balancing test to determine joint employer status that looks at whether the potential joint employer: 1) hires or fires the employee; 2) supervises and controls the employee's work schedule or conditions of employment to a substantial degree; 3) determines the employee's rate and method of payment; and 4) maintains the

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employee's employment records. No one factor is dispositive, but importantly, the employer must have actually exercised one or more of these factors in order to be considered a joint employer. This rule went into effect in March 2020.

The decision from SDNY struck this rule as it applies to "vertical" employment relationships, e.g. those in which an employee works for one employer but another entity or individual simultaneously benefits from that work, but did not strike the rule with regard to "horizontal" relationships, or those in which two related entities both employ or share control of a single employee. While horizontal relationships will continue to be subject to the stringent test contained in the DOL rule, the Court found that the rule's requirement that the potential joint-employer actually exercise control over the employee (as opposed to theoretical control) conflicts with the language of the FLSA with regard to vertical employment relationships. Further, while the factors demonstrating control outlined above are relevant, they are not a necessary condition to establishing liability according to the Court. The Court also found that the DOL did not provide sufficient reasoning to depart from existing legislative history and prior interpretations of the statute, making the rule arbitrary and capricious.

IMPACT ON INDUSTRY: This decision therefore opens the door for increased employer liability, but it is likely to be appealed. Therefore, employers are advised to first determine whether they have any vertical employment relationships (as only those will be affected by this decision) and consult with counsel before taking any measures in response to the new rule and decision. Employers with vertical employment relationships that made significant changes to their employment structures as a result of DOL's final rule are more likely to be affected by this decision and should carefully review those policies for potential liabilities. Vertical employment relationships are also significantly more common in certain industries, such as government contractors. For example, a prime contractor that has a contract to maintain the Pentagon may subcontract with a painter to repaint offices as needed. Depending on how the subcontract is administered, the prime may find itself a joint employer of the subcontractor's painters. Following the SDNY decision, the prime does not need to actually exercise control over the painters, but if it has theoretical control, it may find itself liable as a joint employer. As this example illustrates, even if this decision does not immediately impact a workforce, all employers should take care in structuring future business relationships.

Again, DOL is expected to appeal the decision, but the litigation process will be slow. Wiley's team of employment attorneys is monitoring the issue and will provide additional updates when there are additional developments.