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Months After DOL Issues New "Joint Employer" Rule, Federal Judge Strikes It Down

Earlier this year, the U.S. Department of Labor (DOL) issued a new rule for determining when two businesses are joint employers of the same employee under the Fair Labor Standards Act (FLSA), making it harder to find that one business is the joint employer of another's employee. On September 8, however, a federal judge determined that much of that DOL rule is invalid.

As we explained this past July, the DOL rule identifies two types of scenarios in which a business may be found to be a joint employer. In one scenario, an employer employs an employee to work but another person or entity simultaneously benefits from that work (a so-called vertical joint employment relationship, such as franchisor/franchisee or general contractor/subcontractor). In the other scenario, an employer employs a worker for one set of hours in a workweek and another employer employs the same worker for a separate set of hours in the same workweek (a so-called horizontal joint employment relationship).

Shortly after the DOL issued its new joint employer rule, 18 states sued to invalidate it. In the September 8 decision, Judge Gregory H. Woods of the U.S. District Court for the Southern District of New York ruled that the portion of the rule concerning vertical joint employment is invalid because it conflicts with the FLSA—the federal statute the rule was supposed to be interpreting—and because it is arbitrary and capricious.

Under the DOL rule, to find joint employment via a vertical relationship, the potential joint employer would have to exercise direct or indirect control over the employee. That is analyzed under a four-factor balancing test 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 employee's employment records. Judge Woods described those four factors as "a proxy for control," based on the common-law definition of an employer.

In finding the vertical joint employment rule invalid because it conflicts with the FLSA, Judge Woods opined that the rule incorrectly relied on a potential joint employer's control over an employee, because the FLSA had rejected control as the standard for determining employment. Rather, the court ruled, a determination of whether one is a joint employer under the FLSA must take into consideration the statute's broader definition of "employ" as "to suffer or permit to work." The court noted that the FLSA does not distinguish between employers and joint employers, so the same factors that are relevant in determining whether one is an employer are also relevant in determining whether one is a joint employer. Because the DOL is required to give effect to federal statutes such as the FLSA, concluding that the rule conflicts with the FLSA renders the rule invalid. The court also concluded that the rule contradicts the DOL's own previous understanding of how to determine whether one is a joint employer, including the rule's instruction that whether an employee is economically dependent on a potential joint employer is not relevant to the joint employer inquiry.

In addition to concluding that the DOL's vertical joint employer rule is invalid because it conflicts with the FLSA, the court also found the rule invalid because it is arbitrary and capricious in three respects. First, the DOL did not explain why it departed from its prior interpretations of joint employment. Second, the DOL did not consider a conflict between the rule and regulations it had adopted under another statute, the Migrant and Seasonal Agricultural Workers Protection Act, which defined joint employment differently. Third, the DOL did not consider the cost the rule would impose on workers in potentially reducing their ability to collect back wages owed to them.

The joint employer doctrine long predates the rule issued by the DOL earlier this year. Before the new rule, different courts used different tests to determine whether two businesses were joint employers, including an "economic realities" test that looked at multiple factors to determine whether an employment relationship existed based on a worker's economic dependence on a purported employer. In adopting the new joint employer rule, the DOL emphasized the benefits of one uniform joint employment standard that would apply throughout the country. With the invalidation of the rule's vertical joint employment standard, the inconsistent treatment of that issue among courts returns.

In finding the DOL's joint employer rule invalid with respect to vertical joint employer relationships, the court noted that it was not implying that the DOL cannot make any such rule at all. Rather, the court said, the DOL could issue a new rule, but it would have to be consistent with the FLSA, explain any inconsistency with the DOL's prior interpretation of joint employment, consider potential costs to workers and explain why the benefits of the new rule outweigh those costs.

The court's decision did not invalidate the portion of the DOL rule concerning horizontal joint employment, which made only non-substantive changes to the previous standard. In that scenario, if two employers are sufficiently associated with respect to the employment of an employee, they are joint employers and must aggregate the hours worked for each in determining compliance with the FLSA. Two employers will generally be sufficiently associated to be considered joint employers if (1) there is an arrangement between them to share the employee's services; (2) one employer is acting directly or indirectly in the interest of the other employer in relation to the employee; or (3) the two employers share control of the employee, directly or indirectly, because one employer controls, is controlled by or is under common control of the other employer.

It is not yet known how the DOL will respond to the decision invalidating its joint employer rule, including potentially issuing a new rule in its place. In the meantime, employers should be mindful that the economic realities test and other standards that predated the DOL's rule will determine whether one is a joint employer. Employers with questions about whether those standards apply in any particular case should consult with employment counsel.

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