Updates
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NY Court Strikes Down Significant Portions of DOL’s Final Rule Defining Joint Employment Scenarios Under FLSA

The U.S. Department of Labor's (DOL) Final Rule revising the joint employer regulations under the federal Fair Labor Standards Act (FLSA) took effect on March 16, 2020, (Final Rule). On September 8, 2020, the Hon. Gregory H. Woods, of the U.S. District Court for the Southern District of New York, case no: 1-20-cv-01689-GHW, struck down significant portions of the Final Rule. While the Final Rule claimed to provide "clarity," employers will be left wondering how to evaluate their vertical joint employment relationships.

Summary of the DOL's Final Rule

The Final Rule identified two scenarios under the FLSA, which the court referred to as "vertical" or "horizontal" joint employment.

"Vertical" joint employment typically arises when an entity utilizes a staffing agency, subcontractor, labor provider, or other intermediary employer to provide labor. To determine whether a vertical joint employment relationship exists, the Final Rule applies a four-factor test, focused on whether the putative joint employer: "(i) Hires or fires the employee; (ii) Supervises and controls the employee's work schedule or conditions of employment to a substantial degree; (iii) Determines the employee's rate and method of payment; and (iv) Maintains the employee's employment records." 29 C.F.R. § 791.2(a)(1)(v)-(iv). The Final Rule suggests considering additional factors "only if they are indicia of whether the potential joint employer exercises significant control over the terms and conditions of the employee's work." 29 C.F.R. § 791.2(b).

The second scenario, "horizontal" joint employment, occurs when "one 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. The jobs and the hours worked for each employer are separate, but if the employers are joint employers, both employers are jointly and severally liable for all of the hours the employee worked for them in the workweek." 29 C.F.R. § 791.2(e)(1).

The Procedural History of the New York Lawsuit

Following the DOL's Final Rule, 18 states filed suit, alleging the Final Rule was invalid under the Administrative Procedure Act (APA)[1] and seeking to vacate and enjoin its further implementation. At issue in the court's September 8, 2020, order were the parties' cross motions for summary judgment.

The Court's Holding

In a thorough and lengthy opinion, the court granted in part and denied in part the motions for summary judgment. The court agreed that the Final Rule's vertical joint employer standard was, in fact, "arbitrary and capricious," thus vacating the majority of 29 C.F.R. § 791.2. However, the court allowed the horizontal joint employer scenario at 29 C.F.R. § 791.2(e) to remain in effect. The rationale behind these holdings is explained further below.

The Vertical Joint Employer Standard Conflicted With the FLSA

The court identified three primary ways the Final Rule conflicted with the FLSA.

1. Although the FLSA contains definitions of employer, employ, and employee, the Final Rule relied on the FLSA's definition of "employer" as the "sole textual basis for joint employer liability." According to the court, "all three definitions are relevant to determining joint employer status under the FLSA, and the FLSA's definition of 'employer' cannot be read untethered from its related definitions of 'employee' and 'employ.'"
2. The Final Rule's four-factor test is "a proxy for control." While control is the most important factor in evaluating an employment relationship under common law, the FLSA rejects the common law approach, and has utilized a broader definition of "employer." Accordingly, the Final Rule's emphasis on control is "unduly narrow."
3. The Final Rule improperly limits the factors the DOL will consider in the joint employer analysis, thus contradicting caselaw and the DOL's prior interpretations.

The Final Rule Reached Conclusions That Were "Arbitrary and Capricious"

In addition to finding conflict with the FLSA, the court also ruled that portions of the Final Rule must be set aside because they are arbitrary and capricious. In so finding, the court determined that the Final Rule: (1) failed to explain its departure from DOL's prior interpretations; (2) did not acknowledge or explain the conflict between it and regulations under the Migrant and Seasonal Agricultural Workers Protection Act (with which the joint employer test is supposed to be consistent); and (3) did not adequately contemplate the Final Rule's cost to workers.

Based on the above findings, the court vacated the Final Rule's "novel standard for vertical joint employer liability" but left the "'non-substantive revisions' to existing law for horizontal joint employer liability" in effect. Notably, the court provided guidance on what future rulemaking should look like in the context of joint employer relationships:

"[a]ny future rulemaking must adhere to the text of the FLSA and Supreme Court precedent. If the Department departs from its prior interpretation, it must explain why. And it must make more than a perfunctory attempt to consider important costs, including costs to workers, and explain why the benefits of the new rule outweigh these costs. Because the Final Rule does none of these things, it is legally infirm."

What Does This Mean Going Forward?

Now that the court has invalidated significant aspects of the DOL's Final Rule, the question remains, how should employers respond? We anticipate the DOL will appeal the court's decision and attempt to continue enforcing its Final Rule. However, until the district court's opinion is overruled, employers in potential vertical joint employment scenarios (for example, those who utilize staffing agencies, subcontractors, labor providers, or other intermediaries to provide labor services), will be well served to avoid reliance on the Final Rule in evaluating joint employer status. Employers who have relied on the four-prong test under the first scenario of the DOL's Final Rule and/or focused on elements relating to control may wish to reevaluate their determinations and confirm their decisions have support in case law and/or DOL interpretations that were in effect prior to the Final Rule.

Employers with questions regarding the joint employer analysis under the FLSA should contact counsel. Perkins Coie's labor and employment attorneys are well-positioned to help in this regard.

Endnotes

[1] The APA "sets forth the procedures by which federal agencies are accountable to the public and their actions subject to review by the courts." Agency actions that are "arbitrary" or "capricious" can be "set aside" pursuant to the APA.

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