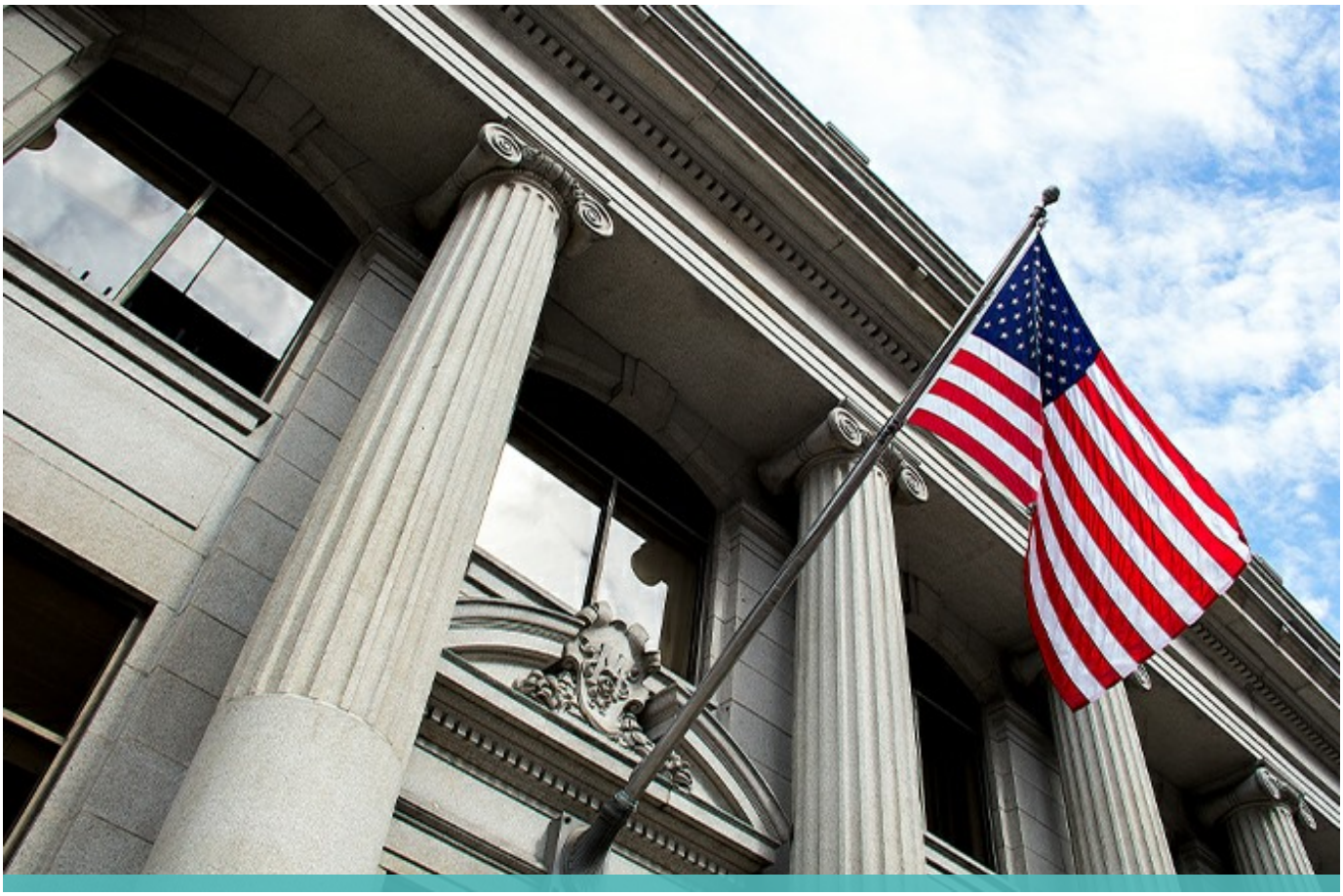
New York court's decision strikes down key portions of new joint employer standard, impacting franchise relationships



Maria G. Carr | Thursday, December 3, 2020

We have previously addressed the ever-evolving changes in the joint employer standard throughout the last few years, but a recent decision by a New York federal court, in the case titled *New York v. Scalia*, Case No. 20-cv-1689-GHW (S.D.N.Y. Sept. 8, 2020), has cast doubt on the new standard that the Department of Labor established earlier this year – one that was originally meant to dispel confusion and clear up the standard.

"Joint employers" are those employers who can be held jointly liable for violations of the Fair Labor Standards Act and other labor laws, and they are commonly applied to franchisor/franchisee relationships. In March 2020, the Department of Labor's revised final rule regarding the joint employer standard took effect, and this rule primarily revised the standard for "vertical" joint employer liability.

"Vertical" joint employment primarily affects franchise relationships – these situations involve instances where an individual is employed by one entity, but may be acting under the direction of another entity. The individual may try to argue that both entities are "joint employers" and are responsible for violations of wage laws. The final rule issued in March 2020 by the Department of Labor was meant to dispel any ambiguity about the situation and narrow the definition of "joint employers." This rule held that another entity is an employee's joint employer "only if that person is acting directly or indirectly in the interest of the employer in relation to the employee." 29 C.F.R. § 791.2(a)(1) (citing 29 U.S.C. §§ 203(e)(1)).

The new rule adopted a four-factor balancing test to make this determination that focuses primarily on the control of the employee, including an evaluation of whether the potential 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)(i)-(iv).

Other factors, like financial dependence between the two entities or an existing franchise relationship, were held to be irrelevant. As a result, this rule was favorable to franchisors – under this standard, franchisors were unlikely to be held to be joint employers of their franchisee's employees unless they exercised substantial control over the employees.

A number of states sued to abandon this final rule, however, because it conflicted with the broad definition of "employer" and "employee" in the Fair Labor Standards Act (the "FLSA"). The FLSA includes very broad definitions of these terms, defining "employee" as "an individual employed by an employer" and an "employer" as "any person acting directly or indirectly in the interest of an employer in relation to an employee." 29 U.S.C. § 203(d-e). Further, the definition of "employ" under the FLSA means to "to suffer or permit to work." 29 U.S.C. § 203(g).

The District Court for the Southern District of New York found that the new final rule that focuses on control was much too narrow and contrasted with these broad definitions – the determination of whether two entities are joint employers does not just focus on "control," but includes an evaluation of a number of factors, including "a consideration of the total employment situation and the economic realities of the work relationship." *New York v. Scalia*, citing *In re Enterprise Rent-a-Car Wage & Hour Emp't Pracs. Litig. (Enterprise)*, 683 F.3d 462, 468-69 (3d Cir. 2012). This may include an evaluation of any number of factors that are not set, including, but not limited to, an established franchise relationship, the power to hire and fire, maintenance of employment records, and certain other factors (none of which is dispositive).

The Court found that the final rule's unjustified elimination of other factors, along with the focus on control, inappropriately ignored prior case law, had the potential to increase enforcement costs, and contrasts with the idea that indirect control over an individual can be sufficient for joint employer status.

The decision was not appealed, but the opinion of the Southern District of New York means that ongoing debate regarding joint employer status is not yet settled. As a result, franchisees and franchisors, along with other entities with the potential for joint employer status, must be careful to continue to evaluate their relationships to avoid potential joint liability for any wage law violations.

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