FLSA Developments:

Misclassification as Independent Contractors, Unpaid Interns, the Status of DOL Opinion Letters, and the Meaning of Clothes Under Section 3(o)

by

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FLSA DEVELOPMENTS

by Robert B. Fitzpatrick, Esq.[1]

MISCLASSIFICATION AS INDEPENDENT CONTRACTORS

1. August 2009 GAO Report to Congress: Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention

    a. "In fiscal year 2007, states uncovered at least 150,000 workers who may not have received protections and benefits to which they were entitled because their employers misclassified them as independent contractors when they should have been classified as employees."

    b. The GAO report is a*vailable at* http://www.gao.gov/new.items/d09717.pdf.

2. The Obama Administration's proposed budget includes a joint proposal by the Department of Labor and the Department of the Treasury to pursue employers that misclassify workers as independent contractors:

    a. Delaware Employment Law Blog, Will "Misclassification Incentives" Reduce Employers' Use of Independent Contractors?, Posted by Scott A. Holt on Feb. 12, 2010, *available at* http://www.delawareemploymentlawblog.com/2010/02/will_misclassification_initiat_1.html?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+delawareemploymentlawblog%2FUagR+%28Delaware+Employment+Law+Blog%29.

    b. Hunton & Williams LLP, Proposed Federal Budget Targets Misclassification of Contractors, Posted on Feb. 12, 2010, *available at* http://www.huntonlaborblog.com/2010/02/articles/employeeindependent-contractor/proposed-federal-budget-targets-misclassification-of-contractors/?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+HuntonEmploymentLaborLawPerspectives+%28Hunton+Employment+%26+Labor+Law+Perspectives%29.

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[1] This article was prepared with assistance by Donald R. McIntosh, an associate with Robert B. Fitzpatrick, PLLC. Mr. McIntosh is a May 2008 graduate of Georgetown University Law Center and a member of the Virginia State Bar.

3. The IRS has entered into information sharing agreements with 29 state labor agencies through which the IRS and the agencies will share results from misclassification audits.

    a. Dave Gram, IRS, States Crack Down on Independent Worker Abuse, The Associated Press, Feb. 11, 2010, *available at* http://www.google.com/hostednews/ap/article/ALeqM5hdqC3b6B0eL-uQlC7O_sJPB7qNmAD9DQ5KL80.

    b. Richard J. Reibstein, et al., Independent Contractor High Alert – The IRS and State Labor Departments Take Aim at Employee Misclassifications: How Employers Can Minimize Their Liability Risks, WolfBlock.com, HRAdvisor (January/February 2008), *available at* http://www.wolfblock.com/wbroot/files/Publication/Reib_Nix_Gall_HRAdvisor.pdf.

4. The Taxpayer Responsibility, Accountability, and Consistency Act of 2009, S. 2882, 111th Cong. (2009) (introduced by Sen. Kerry (D-MA); companion House bill, H.R. 3408, introduced by Rep. McDermott (D-WA)), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:s2882is.txt.pdf.

5. The Independent Contractor Proper Classification Act, S. 2044, 110th Cong. (2007) (introduced by then-Sen.. Obama (D-IL)), *available at* http://www.appwp.org/documents/s2044110th.pdf.

6. The Maryland Workplace Fraud Act, Code of Md. Regs. § 395.10, provides for new penalties for employers that misclassify workers, focusing on the landscaping and construction industries.

    a. A discussion of the Act is *available at* http://www.dllr.state.md.us/workplace/.

7. The Illinois Department of Labor ("IDOL") recently on behalf of 18 individuals issued a civil penalty of $328,500 under the Illinois Employee Classification Act ("ECA"), against Elmwood Park, IL-based Mega Builders, Inc., for failing to classify the individuals as employees.

    a. IDOL assessed penalties of $1,500 per day for 218 total days of misclassification, as well as a $1,500 penalty for failure to maintain proper records.

    b. For the Illinois ECA, *see* State of Illinois Department of Labor, Employee Classification Act, http://www.state.il.us/agency/idol/laws/Law185.htm.

8. On May 25, Ohio H.B. 523 was introduced. This bill would create a single definition of "employee" that would be used in all Ohio statutes. The bill would also create a seven factor test, all of which would have to be met, for determining whether an individual is an independent contractor. The factors are:

- The individual has been and continues to be free from control and direction in connection with the performance of the service.
- The individual customarily is engaged in an independently established trade, occupation, profession, or business of the same nature of the trade, occupation, profession, or business involved in the service performed.
- The individual is a separate and distinct business entity from the entity for which the service is being performed or, if the individual is providing construction services and is a sole proprietorship or partnership, the individual is a legitimate sole proprietorship or a partner in a legitimate partnership.
- The individual incurs the main expenses and has continuing or recurring business liabilities related to the service performed.
- The individual is liable for breach of contract for failure to complete the service.
- An agreement, written or oral, express or implied, exists describing the service to be performed, the payment the individual will receive for performance of the service, and the time frame for completion of the service.
- The service performed by the individual is outside of the usual course of business of the employer.

a. The text of Ohio H.B. 523 is available at http://www.legislature.state.oh.us/bills.cfm?ID=128_HB_523

b. For a discussion of Ohio H.B. 523, see Brian Hall, Ohio H.B. 523 Would Unify Definition of Employee, Make it Easier to Find Misclassification, May 28, 2010, *available at* http://www.employerlawreport.com/2010/05/articles/workforce-strategies/ohio-hb-523-would-unify-definition-of-employee-make-it-easier-to-find-misclassification/

9. Florida Statues Ch. 440 requires employers with 4 or more employees, or if a construction industry employer, one or more employees, to provide workers' compensation coverage for all employees.

a. Fl. Stat. Ch. 440(c)(2) – "Employee" includes: An independent contractor working or performing services in the construction industry. The 2009 Florida Statutes, available at http://www.leg.state.fl.us/Statutes/index.cfm?App_mode=Display_Statute&Search_String=&URL=Ch0440/Sec02.HTM.

b. For a discussion of the above, see Florida Workers' Compensation Joint Underwriting Association, Inc., Helpful Tips for Employers, available at http://www.fwcjua.com/Employer/HelpfulTips.aspx.

10. Is there a potential for RICO claims?

a. *Mohawk Indus. v. Williams*, 568 F.3d 1350 (11th Cir. 2009).

b. *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451 (2007).

11. The “Control” Test v. The “Relative Nature of Work” Test

   a. *Haynie v. Tideland Welding Serv.*, 631 F.3d 1242 (5th Cir. 1980).

   b. Larson, Workers’ Compensation Law §§ 43.53—43.54 (1978).

12. Independent Contractors Covered by the Rehabilitation Act

   a. *Fleming v. Yuma Reg’l Med. Ctr.*, 587 F.3d 938 (9th Cir. 2009).

   b. Tresa Baldas, 9th Circuit Widens Split on Rights of Independent Contractors, Nat’l L.J., Nov. 30, 2009, available at http://www.law.com/jsp/article.jsp?id=1202435862625.

13. Richard B. Cohen & Barri Frankfurter, Employment Discrimination and Its Evolving Impact on an Employer's Relationship with Independent Contractors, Bloomberg Law Reports, Vol. 3, No. 47 (2009), available at http://www.foxrothschild.com/uploadedFiles/newspublications/cohenFrankfurter_employmentDiscriminationEvolving_120709.pdf.

14. DOL’s Proposed “Employee Misclassification Initiative”

   a. Testifying before the House Committee on Appropriations’ Subcommittee on Labor, Health and Human Services, Education, and Related Agencies, Department of Labor Secretary Hilda Solis announced DOL’s proposed “Employee Misclassification Initiative.” *Available at* http://www.dol.gov/_sec/media/congress/20100310_appropriations.htm. The Initiative would provide the following:

      i. $12 million and 90 new investigators for DOL’s Wage and Hour Division to “ensure that workers are employed in compliance with the laws we enforce”;
      ii. Support for “new, targeted [Employee and Training Administration] efforts to recoup unpaid payroll taxes due to misclassification and promote the innovative work of States on this problem,” including $10.9 million for a pilot program awarding States that successfully “detect[] and prosecut[e] employers that fail to pay their fair share of taxes due to misclassification and other illegal tax schemes that deny the Federal and State [Unemployment Insurance] Trust Funds hundreds of millions of dollars annually”;
      iii. $1.6 million for DOL’s Office of the Solicitor and allocating 10 employees to “support enforcement strategies, with a focus on coordination with the States on litigation involving the largest multi-State employers who routinely abuse independent contractor status”;

iv. $150,000 for OSHA to "train inspectors on worker misclassification issues"; and
v. Proposed legislative changes that would "require employers to properly classify their workers, provide penalties when they do not, and restore protections for employees who have been classified improperly."

15. Mark Toth, General Counsel for Manpower, Inc., has created an independent contractor checklist available at http://manpowerblogs.com/toth/wp-content/uploads/2010/05/Blawg-IC-Cheat-Sheet-5.10.pdf.

16. <u>The Employee Misclassification Prevention Act</u> (S. 3254 and H.R. 5107)

a. The Act proposes to do the following:

i. Amend the FLSA to render worker misclassifications a violation of federal law.
ii. Require employers to maintain records reflecting hours worked and wages paid for employees and non-employee workers.
iii. Require employers to provide workers a notice identifying the workers' classification, a DOL website (to be created), contact information for the appropriate DOL office, and any other information as to be required by regulation.
iv. Additionally, for workers classified as non-employees, the notice would be required to include the following: "Your rights to wage, hour, and other labor protections depend upon your proper classification as an employee or non-employee. If you have any other questions or concerns about how you have been classified or suspect that you may have been misclassified, contact the U.S. Department of Labor."
v. Employees who violate the notice and/or recordkeeping requirements or misclassify a worker would be subject to a civil penalty of up to $1,100 per work on the first offense and up to $5,000 for willful or repeated violations.
vi. Employers misclassifying workers and violating minimum wage/overtime requirements could be subject to treble damages.
vii. Provide broad anti-retaliation and discrimination protections.

b. On June 17, 2010, the Senate Committee on Health, Education, Labor, and Pensions held a hearing on the Employee Misclassification Prevention Act, entitled, "Leveling the Playing Field: Protecting Workers and Businesses Affected by Misclassification." Testifying were Seth Harris, the Deputy Secretary of Labor; Frank Battagliano of Metro Test and Balance; Catherine Ruckelshaus of the National Employment Law Project; and Gary Uber of Family Private Care, a home health caregivers referral service. The hearing's prepared testimony and video replay are *available at* http://help.senate.gov/hearings/hearing/?id=225aa689-5056-9502-5d83-96cd13339413.

UNPAID INTERNS

1. In an April 2, 2010 New York Times article, Nancy J. Leppink, DOL's Acting Director of its Wage & Hour Division, rattled the world of unpaid internships when she was quoted as stating the following:

   > "If you're a for-profit employer or you want to pursue an internship with a for-profit employer, there aren't going to be many circumstances where you can have an internship and not be paid and still be in compliance with the law."

   a. The article is *available at* http://www.nytimes.com/2010/04/03/business/03intern.html.

2. Ms. Leppink cited to a Wage & Hour Division's "fact sheet" (*available at* http://www.dol.gov/whd/regs/compliance/whdfs71.pdf) that provides a six-part test for "for-profit" employers to determine whether an internship need be paid. If the six-part test is met, an employment relationship does not exist under the FLSA, and minimum wage and overtime provisions do not apply to the intern. WH Op. Letter FLSA2004-5NA (May 17, 2004); WH Op. Letter 254 (Feb. 22, 1974); DOL Field Operations Handbook § 10b11.

   a. The six-part test is as follows:

      i. **The internship, even though it includes actual operation of the facilities of the employer, is similar to training which would be given in an educational environment**;

         - On this factor, the fact sheet further advises:

           In general, the more an internship program is structured around a classroom or academic experience as opposed to the employer's actual operations, the more likely the internship will be viewed as an extension of the individual's educational experience (this often occurs where a college or university exercises oversight over the internship program and provides educational credit). The more the internship provides the individual with skills that can be used in multiple employment settings, as opposed to skills particular to one employer's operation, the more likely the intern would be viewed as receiving training. Under these circumstances the intern does not perform the routine work of the business on a regular and recurring basis, and the business is not dependent upon the work of the intern. On the other hand, if the interns are engaged in the operations of the employer or are performing productive work (for example, filing, performing other clerical work, or assisting customers), then the fact that they may be receiving some benefits in the form of a new skill or improved work habits will not exclude

them from the FLSA's minimum wage and overtime requirements because the employer benefits from the interns' work.

ii. **The internship experience is for the benefit of the intern**;

iii. **The intern does not displace regular employees, but works under close supervision of existing staff**;

- The fact sheet further advises:

  If an employer uses interns as substitutes for regular workers or to augment its existing workforce during specific time periods, these interns should be paid at least the minimum wage and overtime compensation for hours worked over forty in a work week. If the employer would have hired additional employees or required existing staff to work additional hours had the interns not performed the work, then the interns will be viewed as employees and entitled compensation under the FLSA. Conversely, if the employer is providing job shadowing opportunities that allow an intern to learn certain functions under the close and constant supervision of regular employees, but the intern performs no or minimal work, the activity is more likely to be viewed as a bona fide education experience. On the other hand, if the intern receives the same level of supervision as the employer's regular workforce, this would suggest an employment relationship, rather than training.

iv. **The employer that provides the training derives no immediate advantage from the activities of the intern; and on occasion its operations may actually be impeded**;

v. **The intern is not necessarily entitled to a job at the conclusion of the internship**; and

- The fact sheet further advises:

  The internship should be of a fixed duration, established prior to the outset of the internship. Further, unpaid internships generally should not be used by the employer as a trial period for individuals seeking employment at the conclusion of the internship period. If an intern is placed with the employer for a trial period with the expectation that he or she will then be hired on a permanent basis, that individual generally would be considered an employee under the FLSA.

vi. **The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship**.

3. For more information on these unpaid intern developments, *see, e.g.*:

    a. David Yamada, *The Employment Law Rights of Student Interns*, 35 Conn. L. Rev. 215 (2002).

    b. Workplace Prof Blog, *Unpaid Internships*, April 4, 2010, *available at* http://lawprofessors.typepad.com/laborprof_blog/2010/04/unpaid-internships.html.

    c. Minding the Workplace, *News Flash! Unpaid Internships May Be Illegal*, April 3, 2010, *available at* http://newworkplace.wordpress.com/2010/04/03/news-flash-unpaid-internships-may-be-illegal/.

STATUS OF DOL OPINION LETTERS

1. On March 24, 2010, DOL's Wage & Hour Division released its first "Administrator Interpretation," in which it found that employees who perform the typical job duties of a mortgage loan officer do not qualify as bona fide administrative employees exempt under the provisions of the FLSA Administrator Interpretation, No. 2010-1, Mar. 24, 2010, *available at* http://www.dol.gov/WHD/opinion/adminIntrprtn/FLSA/2010/FLSAAI2010_1.pdf. Simultaneous to this finding, DOL announced that Administrator Interpretations will replace the formerly used opinion letters, which were geared towards addressing detailed, fact-specific situations under the FLSA and other statutes.

2. The Wage & Hour Division's move towards these Administrator Interpretations was predicated on the belief that they "will be a much more efficient and productive use of resources than attempting to provide definitive opinion letters in response to fact-specific requests submitted by individuals and organizations, where a slight difference in the assumed facts may result in a different outcome." U.S. Dep't of Labor, Wage & Hour Division, *Rulings and Interpretations*, *available at* http://www.dol.gov/whd/opinion/opinion.htm.

3. Seyfarth Shaw, in its "One Minute Memo" of March 26, 2010, entitled *DOL Eliminates Issuance of Wage & Hour Opinion Letters While Finding Mortgage Loan Officers Non-Exempt Contrary to Prior Administration Rulings*, provides the following analysis of DOL's decision to eliminate its use of opinion letters:

> The substance of WHD's guidance and WHD's departure from the practice of issuing individual Opinion Letters should be troubling to employers in many industries. As an initial matter, employers have long submitted individualized, fact-specific inquiries and relied on responsive Opinion Letters as part of their good-faith efforts to comply with wage-and-hour laws. Indeed, the Portal-to-Portal Act provides that an employer is not subject to liability, including liquidated damages, under the FLSA if it can establish good-faith reliance on a "written administrative regulation, order, ruling, approval, or interpretation" of WHD. There is presently a backlog of approximately 400 requests for Opinion Letters.
>
> Moreover, the AI, in contrast to prior WHD Opinion Letters, lacks any transparent factual inquiry and instead relies upon WHD's generalized understanding of the duties that commonly accompany a position in an industry. Yet, for years, WHD has acknowledged that job titles alone are not dispositive in determining whether an exemption applies and recognized that the law requires a specific factual inquiry to be conducted into the actual duties an employee performed. Likewise, prior Opinion

Letters have taken account of the reality that actual duties performed in a particular position often vary.

4. On May 20, 2010, in response to a request for an explanation of the delegation which gives the Deputy Wage and Hour Administrator power to issue Administrator Interpretations, the Acting Deputy Administrator for Enforcement claimed this power was found in Secretary's Order 9-2009 (published at 74 Fed. Reg. 58836 (Nov. 13, 2009)). That order delegated the responsibility of issuing official departmental rulings and interpretations of the FLSA to the Wage and Hour Administrator. When, as is the case now, there is no Administrator, the Administrator's duties fall to the Administrator's "first assistant" under the Federal Vacancies Reform Act of 1998. 5. U.S.C. § 3345, et seq. The Secretary of Labor has designated the Deputy Wage and Hour Administrator as the "first assistant" to the Wage and Hour Administrator. Secretary's Order 04-2008 (published at Fed. Reg. 46524, 46527 (Aug. 8, 2008)). Thus, until the position of Wage and Hour Administrator is filled, the Deputy Wage and Hour Administrator has the authority to issue Administrator Interpretations.

Meaning of Clothes Under Section 3(o)

1. On June 16, 2010, the Wage and Hour Division issued Administrator's Interpretation No. 2010-2. This interpretation states that "the § 203(o) exemption does not extend to protective equipment worn by employees that is required by law, by the employer, or due to the nature of the job." This interpretation of the meaning of clothes overrules both a 2002 and 2007 opinion letter stating that protective equipment was included in the meaning of "clothes." Thus, employers must now compensate unionized employees for time spent putting on and taking off protective gear regardless of any collective bargaining agreements.

2. The Administrator's Interpretation also concluded that "clothes changing covered by § 203(o) may be a principal activity." Thus, under the Portal to Portal Act, 29 U.S.C. § 254, changing clothes can now trigger the start of a work day and compensable work time.

3. The Administrator's Opinion is *available at* http://www.dol.gov/whd/opinion/adminIntrprtn/FLSA/2010/FLSAAI2010_2.htm.

4. For further discussion of these topics, see:

    - Thompson, *FLSA Clothes-Changing Exception Doesn't Apply to Protective Gear, Says DOL*, June 16, 2010, *available at* http://www.thompson.com/public/newsbrief.jsp?cat=EMPLOYLAW&id=2912

    - Philip Miles, *Redefining Clothes – DOL Edition*, June 16, 2010, *available at* http://www.lawfficespace.com/2010/06/redefining-clothes-dol-edition.html

    - Daniel Schwartz, *DOL Redefines "Clothes" Under Federal Wage & Hour Laws; Now Excludes Protective Equipment Required by Law*, June 16, 2010, *available at* http://www.ctemploymentlawblog.com/2010/06/articles/wage-and-hour/dol-redefines-clothes-under-federal-wage-hour-laws-now-excludes-protective-equipment-required-by-law/

    - Shaw Valenza LLP, *US DOL Issues New Administrator Opinion*, June 17, 2010, *available at* http://shawvalenza.blogspot.com/2010/06/us-dol-issues-new-adminstrator.html