SIMPSON▪DELMORE▪GREENE

EMPLOYMENT LAW UPDATE
September 2015

Terence L. Greene
619-702-4308
tgreene@sdgllp.com

Brook T. Barnes
619-702-4307
bbarnes@sdgllp.com

Nicholas J. Ferraro
619-702-4333
nferraro@sdgllp.com

The Department of Labor's "Economic Realities" Test Affects Your Workforce: Time to Review Your Workers' Employment Status

Summary: Earlier this summer, the Department of Labor ("DOL") issued an Administrator's Interpretation (No. 2015-1) that utilized the "economic realities" test to conclude that "most workers classified as independent contractors are employees under the FLSA's broad definitions." While the economic realities test is currently not binding case law, the test employs six factors that we expect California courts and administrative agencies will use to assess claims of misclassification. Employers should carefully review their workers' employment status as the DOL embarks on more enforcement actions and plaintiff's attorneys continue to pursue substantial penalties.

Discussion: The DOL relies upon the "economic realities" test to determine whether a worker has been misclassified as an independent contractor, which is based on the Fair Labor and Standards Act's ("FLSA") "suffer or permit" standard. This means that any worker who is "economically dependent on an employer is suffered or permitted to work by the employer," and thus should be classified as an employee.

The DOL outlines the following factors in the "economic realities" to determine a worker's employment status:

1. Integral to the Employer's Business

The first factor is whether the worker's performance is an "integral part of the employer's business." The DOL concludes that if a worker performs services that the company is in the business of providing, the worker is more likely to be considered an employee. The Interpretation provides an example of a construction company that frames residential homes as its primary business. Because carpenters are integral to the employer's business, they are employees. Conversely, if the construction company contracts with a software developer to create construction bid software, the developer would not be an employee because software development is not the company's primary business. For companies that provide a variety of products or services, this factor may be problematic. The bottom line is that if your company uses an independent contractor that performs the same or similar job functions as your company's employees, then that worker is likely misclassified under the DOL's economic realities test.

2. Managerial Skill Affecting Profit of Loss

The second factor the DOL considers is whether the individual's "managerial skill" affects his or her opportunity for profit or loss. A worker who has the opportunity to hire others or purchase equipment and materials in order to increase his or her profit is more likely to be considered an independent contractor. Conversely, a worker who increases his or her compensation by working more hours and exercises minimal managerial skill is likely an employee. The DOL Interpretation provides an example of a cleaning service where a worker does not schedule his own cleaning assignments or solicit work from other clients, but rather performs cleaning assignments as determined by the company. In such scenarios, the worker does not exercise managerial skill that affects his profit or loss, as his earnings fluctuate based on his completion of the scheduled hours of work. The DOL makes clear that this lack of managerial skill is indicative of an employment relationship between the worker and the company. If your company dictates the "what, where, when, and how" of a worker's daily schedule, then that worker is more likely an employee.

3. Investment Comparison

In the third factor, the DOL examines the nature and extent of the relative investment of the employer and worker in determining the worker's employment status. The DOL's Interpretation provides the same example of a worker at a cleaning service. The worker occasionally brings his own preferred cleaning supplies to certain jobs, but he uses the company's insurance, vehicle, equipment, and supplies. The company invests in advertising and client solicitation. In this scenario, an employment relationship exists because of the relatively minimal investment of the worker (preferred cleaning supplies) compared to the employer's investment (insurance, vehicle, supplies, and advertising). The DOL surmises that the worker's investment in cleaning supplies does little to further a business beyond that particular job; whereas, the company's investment furthers its broader business purposes. Accordingly, we advise employers to carefully audit the level of financial support they provide independent contractors.

4. Special Skill and Initiative

Furthermore, the DOL's Interpretation also suggests that courts and administrative agencies should examine the worker's business skills, judgment, and initiative, rather than his or her technical skills, to determine whether the worker is economically independent. The Interpretation provides an example of a carpenter who does not make any independent judgments at the job site beyond the work that he is doing for that job; he does not determine the sequence of work, order additional materials, or think about bidding the next job, but rather is told when and where to perform specific tasks. In this scenario, the carpenter, although highly-skilled, is not demonstrating the skill and initiative of an independent contractor (such as managerial and business skills). The DOL concludes that he is simply providing his skilled labor and therefore performs his duties in an employment relationship. The DOL's assessment of this factor challenges many independent contractor relationships where a specific skill set is desired by the company: employment recruiters; IT professionals; technical writers; marketing and advertising professionals; and skilled construction workers.

5. Permanent or Indefinite Relationship

The permanency of the relationship between the worker and the company is also a factor in the classification assessment. A long-term relationship between the parties suggests the worker is an employee. For example, an editor who has worked for an established publishing house for several years and whose work is completed in accordance with the publishing house's specifications is most likely in an employment relationship regardless of the freedom and autonomy the company states the editor retains. According to the DOL, an independent contractor, "typically works one project for an employer and does not necessarily work continuously or repeatedly for an employer." Often, companies confuse autonomy and freedom as indicia of an independent contractor relationship: "We don't care how many hours you work as long as the work gets done . . . but you have to show up the office to perform the work the way we specify." Under the economic realities test, it is important that your company pays particular attention to the direction and responsibilities provided to independent contractors.

6. Nature and Degree of Employer's Control

The final factor in the DOL's economic realities test analyzes whether the worker controls meaningful aspects of the work performed such that it is possible to view the worker as a person conducting his or her own business. The DOL specifically states that the "control" factor should not play an outsized role in the analysis of whether a worker is an employee or an independent contractor. The reason for this is to guard against employers who willfully do not inquire about the working conditions of their employees. For example, an employer's lack of control over workers is not particularly telling if the workers work from home. In such cases, the employer permits the offsite work and forsakes direct supervision. The DOL notes that an employer cannot willfully shirk control to avoid an employment relationship.

Concluding Thoughts and Recommended Action

The most important aspect of the DOL's Interpretation is the conclusion: "most workers are employees under the FLSA's broad definition." While the DOL's opinion is the trend in judicial opinions, the Interpretation is not binding case law on California or federal courts. Regardless, we expect courts as well as state and federal agencies will give deference to the Interpretation and its reasoning. As such, companies should review their independent contractor relationships against the interpretations in the memorandum and re-evaluate those relationships vulnerable to the DOL's broad interpretation.

Based on the Interpretation, we recommend the following:

- Do not assume all workers may be classified as independent contractors. Constantly re-assess the classification given the current law and changing work duties and circumstances of the workers;
- Ensure there is an agreement for services with the contractor with specific indemnity provisions addressing wage and hour liability;
- Permit the contractor to take other jobs and expressly state this freedom in the agreement;
- Make the contractor responsible for his or her tools, equipment or supplies;
- Terminate contractors only for material breach or with proper notice under the contract terms;
- Train your employees to communicate properly with contractors and make sure your employees are not directing the means of how the contractor performs his or her work;
- Review whether the contractor has a separate business license, insurance coverage, and contracts with other businesses;
- Contractors should not perform functions that are integral to your business or involve direct service to your customers.

CALIFORNIA LAW: CHEERLEADERS ARE EMPLOYEES

On the issue of employees being misclassified as independent contractors, Governor Jerry Brown recently signed Assembly Bill 202, which requires that professional sports organizations recognize cheerleaders as employees rather than independent contractors. The bill takes effect January 1, 2016.

A Good Rest Period Policy May Not Be Good Enough: Recent Case Increases Employer Responsibility

Summary: The Court of Appeal in *Safeway Inc. v. Superior Court (Esparza)* recently upheld a trial court's class certification on a wage claim case involving employees whose time records reflected lunches of less than 30 minutes on one or more occasions. The court held against Safeway so that employees were permitted to bring claims for premium pay based on Safeway's lack of a policy or practice regarding meal break pay for breaks of less than 30 minutes.

Discussion: Since the California Supreme Court's *Brinker* decision, most California employers know that premium pay is not automatically available to an employee who takes a short lunch break. This is because the *Brinker* court stated that employers do not have an obligation to police its employees to ensure that they take their full 30-minute lunches. The court in *Brinker* made clear that an employer only has to provide its employees the opportunity to take a full 30-minute lunch, and if the employee chooses on his or her own volition to clock in a few minutes early (or skip lunch entirely), the employer is not liable to the employee for any meal break premium.

Indeed, under *Brinker* the employer is only liable for meal break premiums if the employer fails to provide an employee the opportunity to take a 30-minute lunch break, prevents the employee from taking the break, or forces the employee to work through all or part of his or her lunch. For this reason, time records reflecting lunches of less than 30 minutes should not alone mean that an employer is liable for premium pay for failing to provide employees with required meal breaks. However, the *Safeway* decision adds a new consideration to premium pay wage claims.

The facts in *Safeway* are straightforward: the plaintiff brought a class action based upon the theory that Safeway's lack of a policy or practice of reviewing time cards automatically deprived employees of premium pay for short lunches. In a departure from California courts' interpretation of *Brinker*, both the Superior Court and the Court of Appeal held that a class should be certified on this theory. Despite Safeway's efforts to deny class certification by submitting evidence that employees were consistently provided the opportunity to take a full 30-minute meal break, the trial court focused on *Safeway's* failure to automatically pay the premium pay for all short lunches.

The court stated Safeway's failure to pay was unlawful and unfair under California's Unfair Competition Law (Business and Professions Code section 17200). The court made this decision even without common proof of a class-wide failure to provide meal breaks to its employees. The trial court relied on class time records submitted by the plaintiff showing instances of short lunches. The court also relied on declarations wherein some class members testified that they were sometimes unable to take a full 30-minute lunch due to work demands. The trial court concluded that this evidence could support a finding that a policy of never paying premium pay for a missed lunch violated California law because the policy applied in some instances where evidence might show that premium pay had actually been owed due to an employee being prevented from taking a full lunch break.

Despite this speculative finding, the trial court rejected Safeway's position that individualized inquiries would be required to determine whether Safeway failed to provide meal breaks to any particular class member. The trial court granted class certification, and the Court of Appeal affirmed, even though the defendant filed more than 2,000 class member declarations in an effort to oppose certification. The Court of Appeal ultimately concluded that when an employer's records show no meal period taken where one was required, this creates a rebuttable presumption that a violation occurred.

Most importantly, *Safeway* is an instructive case about the need for employers to develop a meaningful review system to avoid potential premium pay liability for missed employee meal and rest periods. We suggest working with counsel to update and renew your meal and rest period policies.

NLRB Joint Employment Ruling Creates Risks for Companies Utilizing "Temps" or Staffing Agencies

Summary: On August 27, National Labor Relations Board ("NLRB") issued its ruling in *Browning-Ferris Industries of California, Inc.* (362 NLRB No. 186), which departs from its long-standing joint employer test in favor of a far more expansive view of joint employment. The decision will likely have substantial implications for companies that utilize temporary staffing agencies and contractors.

Discussion: Browning-Ferris Industries ("Browning") operated a waste recycling facility and employed approximately 60 employees who worked outside the facility. Browning also had a temporary labor service agreement with Leadpoint Business Services ("Leadpoint"), under which Leadpoint provided Browning with approximately 240 workers. The workers were sorters, housekeepers, and cleaners who worked inside the facility. Leadpoint's agreement with Browning contained provisions that required the staffing agency to hire, train, compensate, manage, discipline, review, and terminate its employees. Teamsters Local 350, which already represented the 60 Browning employees, petitioned to represent the 240 workers in negotiations with both Leadpoint and Browning, which the Teamsters argued were joint employers of the workers.

Upon review, the NLRB evaluated (1) whether a common-law employment relationship existed and (2) whether the putative joint employers "possessed sufficient control" over employees' essential terms and conditions of employment. In rendering its decision, the NLRB established a new joint employer standard, whereby "sufficient control" can be established directly or indirectly based on contractual provisions between the two putative joint employers.

Based in part on the following factors, the NLRB found that Browning maintained sufficient control over Leadpoint workers to establish a joint employment relationship:

- Browning set qualification levels for Leadpoint employees; could reject any worker the company referred to its facility; could prohibit Leadpoint from hiring workers Browning previously terminated;
- Browning restricted Leadpoint from paying its employees more than Browning employees who performed the same or similar work;
- Browning maintained control over specific Leadpoint worker employment conditions, such as productivity standards, shift schedules, and employee breaks.

Due to these factors, the *Browning-Ferris* decision ultimately makes it easier for labor unions and employees to establish joint employer status in situations involving temporary employees or staffing agencies. Once joint employment status is established, a company's "temp" workforce can force that company to the collective bargaining table to negotiate the terms and conditions of their employment.

For these reasons, it is imperative that companies that supplement their workforce with contingent employees review their contractual relationships to determine whether those contracts contain provisions that grant the company "sufficient control" over the staffing company's employees. Given the NLRB's recent decision and the Department of Labor's recent memorandum on independent contractors, the savings of utilizing staffing companies must be weighed against the probability of litigation and severity of liability.

White Collar Federal Overtime Exemptions Set to Change in 2016: Get Ahead of the Litigation

Summary: Since our last update, the Department of Labor published a Notice of Proposed Rulemaking ("Notice") that will more than double the minimum salary requirements for a worker to be "exempt" from the FLSA's overtime regulations.

Discussion: Currently under federal law, employers are required to pay time-and-a-half for all employees covered by the FLSA, if those employees work in excess of 40 hours in a single workweek. The FLSA exempts certain executive, administrative, and professional workers from overtime if their job responsibilities satisfy the "duties test" and their pay satisfies the "salary test." Currently, the salary test requires that exempt employees earn more than $23,660 per year or $455 per week. The proposed changes would increase the minimum salary threshold for these exempt workers, requiring employers to pay $50,440 per year or $970 per week to satisfy the executive, administrative, and professional exemption's salary test. Additionally, the proposed changes would also increase the annual salary threshold for the highly compensated employee exemption from $100,000 to $122,148. If adopted, these changes will have an immediate and direct impact on your company.

The DOL is also considering whether the executive, administrative, and profession exemptions' duties tests should be modified to require the employees to perform enumerated duties for least 50 percent of their working time. This standard is similar to the California standard and would impose an additional burden on employers to disseminate clear job duties, monitor performance, and audit employees' working practices. California's exemption requirements remain unaffected as of September 2015.

We will monitor any changes the DOL implements going forward, but we suggest that employers immediately begin internally auditing which employees will be affected by the changes. Please note that simply shifting employees from salary to hourly or from exempt to overtime-eligible could trigger legal liability and disrupt business operations. Contact counsel to develop a plan to manage employees through these regulatory changes.

. . .

This Update was sent to inform clients and interested parties of recent developments in employment law and should not be regarded as a substitute for comprehensive legal advice.

Downtown San Diego
600 West Broadway, Fourth Floor
San Diego, CA 92101
Tel: 619-515-1194
Fax: 619-515-1197

North San Diego
11858 Bernardo Plaza Court, Suite 110
San Diego, CA 92128
Tel: 619-515-1195
Fax: 619-515-1196