Subcontractors and Contingent Workers: Minimizing the Risk of Joint-Employer Liability

Virtually all companies today use subcontractors, independent contractors or consultants, temporaries or other contingent workers to perform certain functions for their businesses. The types of relationships and arrangements vary widely. In some cases, companies hire an independent contractor or consultant because they have special expertise. In other cases, a contractor might hire a professional employer organization, a temp agency or labor provider to reduce administrative or regulatory burdens, overhead or liability. Entire business units are sometimes contracted out. In other cases, temps are viewed as a low risk way to try out potential employees.

Whatever the structure or reason for it, there is no doubt that the use of contingent workers has skyrocketed in recent years.

The law has long recognized contingent worker relationships. Independent contractor relationships have long been recognized, and the common law’s “borrowed servant rule” was an early effort to assign legal responsibility for workers who today might be called “temps.”

For most legal purposes, the common law’s “right of control” test was applied to determine whether an employment relationship existed. That test, which is still in use in some cases, looks at whether the worker is retained to work according to his own methods, and is subject to control only as to the end product or deliverable. The more freedom and responsibility the worker has to determine how the job will be done, the more likely it is that he will be considered an independent contractor instead of an employee.

As the American workplace evolved and regulation of it increased, the legal standards applied to identify employment relationships also evolved. Following passage of the Fair Labor Standards Act (FLSA), for example, the “economic realities” test was developed to identify employees who were entitled to federal minimum wage and overtime protections. That test seeks to determine how economically dependent a worker is on a business to determine whether he is an employee for purposes of the FLSA.
Variations of the “right of control” and the “economic realities” tests have been developed to identify employment relationships under equal employment opportunity laws and regulations, tax laws and regulations, as well as for state workers' compensation and unemployment compensation purposes.

The “joint-employer” concept was developed to determine whether two otherwise independent businesses might both be deemed the employer of a worker or group of workers for certain purposes. The legal standard applied to determine whether two employers should be deemed “joint-employers” for certain purposes have varied over time. Most recently, the National Labor Relations Board (NLRB) and the federal Department of Labor (DOL) made shifts in the standards they apply to determine whether two business are joint-employers.

These developments are discussed below, followed by suggestions that contractors might take to assess the risks of joint-employment and possibly reduce the likelihood of such a finding.

**Joint-employment and the NLRB**

In the Oct. 6, 2015 edition of this CFMA’s Construction Financial Business Management, my partner Stephen Wright discussed the National Labor Relations Board’s recent Browning-Ferris decision. Here, the NLRB abandoned its previous rule that found a joint-employment relationship only where one company actually exercised control over the employees of a second employer. Instead, the Board announced that it would find joint-employment relationships where one employer merely possesses the ability to exercise control over the employees of the other employer.

As that article pointed out, Browning-Ferris makes it much more likely that a contractor can be drawn into a labor disputes involving employees of a subcontractor, a temp agency, or a professional employer organization.

Obviously, being pulled into another employer’s labor dispute is something for which most contractors cannot budget or plan. Taking steps to ensure that a joint-employment relationship does not exist is undoubtedly the best way for a contractor to insulate itself from another employer’s union-related legal issues. With traditional contractor/subcontractor relationships, reducing the likelihood that a joint-employment relationship will be found may be relatively simple.

In contrast, where a contractor uses another employer to supply workers that it directly controls, the likelihood of a joint-employment finding is much greater, and the best approach may be for the contractor to insulate itself as from much potential liability from potential liability.

Many of the suggestions at the end of this article should help reduce the likelihood the risk that a contractor will be deemed a joint-employer in a subcontractor or other business’ labor disputes.

As worrisome as the prospect of a surprise labor dispute might be, more troubling day-to-day risks may be associated with a recent “Administrator’s Interpretation” issued by the federal DOL’s Wage and Hour Division (WHD). That interpretation, and corresponding guidance by the same agency on the Family and Medical Leave Act (FMLA), could substantially increase the potential liability faced by unsuspecting contractors. Given the recent popularity of class and collective action cases alleging wage and hour violations, and the television ads placed by lawyers seeking clients with wage and hour claims, the potential financial risks associated with joint-employment under the FLSA should not be taken lightly.

**Joint-employment under FLSA**

In January, the Administrator of the federal DOL’s WHD issued an official “Administrator’s Interpretation” addressing the joint-employment concept. Interestingly, the report often uses construction industry scenarios
to demonstrate situations where joint-employment relationships might be found.

The report begins by pointing out that, for purposes of the FLSA, the employment relationship is broadly defined. The statute defines an “employee” as “any individual employed by an employer.” The definition of “employ” includes “to suffer or permit to work,” which the U.S. Supreme Court has described as one of the broadest definitions in any statute.

The report also points out that the “economic realities test,” along with the statute’s expansive definition of employment, likely will result in determinations that businesses that might not be employers under the “right of control” test, will nevertheless be employers for purposes of FLSA compliance.

From that foundation, the Administrator goes on to note that the FLSA regulations contemplate the possibility that an individual may be simultaneously employed by two or more employers, and states that the concept of joint-employment, like employment generally, should be defined expansively, ensuring that application of the FLSA will be as broad as possible.

The Administrator discusses two joint-employment types and structures. The first, labeled “horizontal” joint-employment, will exist when the employee works for two (or more) technically separate, but related or overlapping, employers. The focus for determining “horizontal” joint-employment is on the relationship of the businesses involved. Where such a relationship is found, the employee’s work for the joint-employers during a workweek is considered “one employment” rendering the joint-employers jointly and severally liable for compliance with the FLSA, including for paying overtime for all hours worked over 40 in the workweek, regardless of where the overtime hours were worked.

For the construction industry, the more likely joint-employment structure is what the Administrator describes as “vertical” joint-employment. The example used by the Administrator to demonstrate vertical joint-employment relationships is clear: “The vertical joint-employment analysis is used to determine, for example, whether a construction worker who works for a subcontractor is also employed by the general contractor....”

The Administrator goes on to explain that the vertical joint-employment analysis examines the economic realities of the relationships between the construction worker and the general contractor to determine whether the worker is economically dependent on the joint-employers and is therefore the employee of both. If he is, the result could be that the general contractor may be investigated, sued, or otherwise held liable for compliance with the FLSA’s requirements if the subcontractor fails to comply.

The guidance lists seven factors to be considered in determining whether a worker is economically dependent on vertical joint-employers:

- **Directing, Controlling, or Supervising the Work Performed.** The more control the contractor exerts over the work of a subcontractor’s employees, the more likely it is that joint-employment will be found. The sub should run his business and direct his own employees. The exercise of indirect control can also be indicative of joint-employment. For example, if the contractor directs the work of a sub’s employees by issuing specific instructions to the sub’s supervisor, the WHD or a court might find such indirect control sufficient to indicate the employee’s economic dependence on the contractor.

- **Controlling Employment Conditions.** A contractor should not dictate or reserve the right to control terms and conditions of employment of a sub’s employment. For example, a contractor should never hire or fire a sub’s employee, tell the sub what its employees how much its employees must be paid or what benefits they must be provided. Doing so will support a finding that the employee is economically dependent on the contractor.
"Minimizing the Risk of Joint Employer Liability," CFMA Building Profits

- **Permanency and Duration of Relationship.** Simply stated, the longer another’s employee works for a contractor, the more likely it is that the employee is economically dependent upon the contractor.

- **Repetitive and Rote Nature of Work.** A sub’s employees who provide low or no skill work for a contractor are more likely to be deemed economically dependent on the contractor.

- **Integral to Business.** If the work performed by a sub’s employees is an integral part of the contractor/potential joint-employer’s business, it is more likely that the WHD or a court would determine the employee to be economically dependent upon the contractor. This was a key factor in the Browning-Ferris case: the company’s business was waste recycling, and the subcontractor’s employees performed sorting duties – an integral part of the company’s business.

- **Work Performed on Premises.** If the employee works on a site owned or controlled by the contractor/potential joint-employer, the likelihood that a joint-employment relationship will be found to exist is greater.

- **Performing Administrative Functions Commonly Performed by Employers.** The more administrative functions the contractor performs for a sub’s employees, the more likely it is that the contractor will be deemed a joint-employer. For example, if the contractor handles payroll, provides workers’ compensation insurance, sets the work schedules, assigns work and provides training, tools or other equipment for the sub’s employees, it is more likely the contractor will be deemed a joint-employer.

The mission of the WHD is to ensure that covered workers are paid in accordance with the law. The best way a contractor can avoid concerns about whether it is a joint-employer for FLSA purposes, is to ensure that its subcontractors and other direct employers meet or exceed the applicable legal requirements. The suggestions at the end of this article should be helpful in that regard.

**Joint-employment under FMLA**

The federal WHD is also responsible for enforcement of the federal Family and Medical Leave Act (FMLA). It should come as no surprise, then, that the WHD issued guidance in January 2016 regarding joint-employment under the FMLA.

Determining joint-employment for FMLA purposes is the same as under the FLSA. Consequently, all of the factors listed above that might indicate joint-employment under the FLSA, will also be considered to determine responsibility for FMLA compliance.

One potentially important consideration in the FMLA context is that employees who are jointly employed by two employers must be counted by both employers for purposes of determining coverage of the FMLA, and employee eligibility under the FMLA. Assuming both employers are covered by the FMLA, responsibility for compliance will be affected by which is the primary and which is the secondary employer.

In the construction industry, the primary employer for joint-employment purposes will typically be a subcontractor or other labor provider. For FMLA purposes, the primary employer is typically responsible for following all of the FMLA requirements, including giving required notices, providing leave, and maintaining health benefits. The secondary employer, usually the contractor, is prohibited from interfering with a joint employee’s exercise of FMLA rights, or from firing or discriminating against an employee for FMLA-protected activity. The secondary employer might also be responsible for returning or allowing the employee to return to work following FMLA leave, as well as for maintaining records required by the FMLA.
Minimizing Potential Joint-Employer Liability

For purposes of avoiding joint-employment liability, the niceties of a formal legal standard are not of paramount importance. When the question is presented, all of the circumstances will be examined to determine whether a contractor is legally an employer of workers who are nominally employed by another entity.

As much of this article should make clear, subcontracts should clearly provide that the subcontractor is responsible for performing the task for which it was hired, that the subcontractor is solely responsible for manner and means of performance, for hiring, training, supervising and managing its employees, for maintaining discipline and attendance, and for decisions involving termination of employment. Industry standard contracts should not be used without considering the potential impact their terms might have if a joint-employment issue is presented. The contractor should not reserve the right to step in and supervise the work, nor should it do so. Instead, the contractor should ensure that it has the ability to terminate the contract in its entirety if it determines that the work is not being performed satisfactorily. The more detail the contract includes about hiring, wages, work performance and discipline, hours worked or specific work processes, the more likely it is that the contractor will be considered a joint-employer.

The best way for a contractor to protect against liability from a possible joint-employment relationship is to ensure that your subcontractor, PEO, or other labor provider complies with all applicable federal, state, and local employment laws and regulations. The contracts should include broad requirements, not specific wage or overtime restrictions or specifications regarding specific employment terms. If possible, the contract should include requirements that the provider indemnify or hold the contractor harmless for employment-related liability that might arise. It might also require that the provider provide for the legal defense of the contractor in connection with any employment-related action involving employees of the provider. Most contracts do, and obviously should, ensure that adequate workers compensation coverage is in effect. But contractors should also consider requiring that providers obtain employment practices liability insurance.

Finally, management and supervisor training is key. In the end, it doesn’t matter what a written contract says if the contractor’s supervisors in fact exert control over the work of a subcontractor’s employees. Even when it comes to legal issues, actions often speak louder than words.