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PEOs, Staffing Companies: Watch Proposed New Joint Employer Rule

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Professional Employer Organizations, franchisors, business advisors, and staffing agencies should take a close look at their contracts if the Department of Labor's proposed new standard for what constitutes a joint employer becomes final. The proposed rule implements a new four-factor test to evaluate whether a joint employer relationship exists.

The DOL's proposed rule reflects the new administration's narrower perspective of joint employers, and rejects the "not completely disassociated test" (with no definable scope) in favor of a balancing test based on four factors to determine if the potential joint employer:

1. Hires or fires the employee;
2. Supervises and controls the employee's work schedules or conditions of employment;
3. Determines the employee's rate and method of payment; and
4. Maintains the employee's employment records.

The current rule for joint employer status, found at 29 C.F.R. 791.2, is based on whether entities are acting "entirely independent of each other" and are "completely disassociated" with respect to the "employment or a particular employee." This section finds a joint employer relationship in two

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circumstances: (1) when an "employee performs work which simultaneously benefits two or more employers"; and (2) when an employee "works for two or more employers at different times during the workweek," Joint employer relationships generally exist if: (i) there is an arrangement between the employers to share the employee's services, as, for example, to interchange employees; (ii) one employer is acting directly or indirectly in the interest of the other employer (or employers) in relation to the employee; or (iii) the employers directly or indirectly "share control of the employee," because one employer controls, is controlled by, or is under common control with the other employer. In 2017, new DOL Secretary Alexander Acosta withdrew the Wage and Hour Division's 2016 "Administrator's Interpretation" of the current rule that attempted to broaden the joint employment relationship without defining the scope. That AI guidance did not go through the rule-making process that includes public notice and comment.

Notably, under the proposed rule, a court could find the existence of a joint employment relationship even if only one of the four factors is present. The proposed standard applies to either of the two joint employer scenarios codified in Section 791.2 (when an "employee performs work which simultaneously benefits two or more "employers" or when an employee "works for two or more employers at different times during the workweek.")

This proposed rule is the first meaningful revision to the DOL's joint employer regulation since 1958. The opportunity to comment on the proposed rule closed in June.

Examples of the New Joint Employer Proposal

The DOL provided guidance on applying the proposed, four-factor test and clarified its application in particular business relationships, including franchises, business practices advisors/providers, staffing agencies, and certain

contractual relationships. For purposes of this alert, we have provided below two of the six examples in the proposed rule) that seem to most closely parallel a temporary staffing relationship and a PEO arrangement.

Staffing Agency: The following is the example in the proposed rule that describes a staffing agency and its relationship with a client receiving contingent workers assigned by the staffing agency:

> A packaging company requests workers on a daily basis from a staffing agency. The packaging company determines each worker's hourly rate of pay, supervises their work, and uses sophisticated analysis of expected customer demand to continuously adjust the number of workers it requests and the specific hours for each worker, sending workers home depending on workload. Is the packaging company a joint employer of the staffing agency's employees?
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> Under these facts, the packaging company is a joint employer of the staffing agency's employees because it exercises sufficient control over their terms and conditions of employment by setting their rate of pay, supervising their work, and controlling their work schedules.

Clearly, this example directly impacts temporary staffing agencies. Expect users of staffing services and the American Staffing Association to weigh in. If the example holds without material change, also expect customers of staffing services to require specific language in service agreements addressing this example to minimize the chance of joint employer status. Expect also for customers to seek indemnity from the staffing agency for any finding of joint employer status.

Contractual Agreement / PEO: The proposed rule also includes an example that references factors arguably applicable to a PEO arrangement. Although not a PEO, co-employment agreement, this example,

entitled “contractual agreement,” includes a reference to one party reserving of a right to direct and/or control of employees. Many state PEO licensing statutes require a PEO agreement to include such a reservation of rights. Here is the example:

> An office park company hires a janitorial services company to clean the office park building after hours. According to a contractual agreement with the office park and the janitorial company, the office park agrees to pay the janitorial company a fixed fee for these services and reserves the right to supervise the janitorial employees in their performance of those cleaning services. However, office park personnel do not set the janitorial employees’ pay rates or individual schedules and do not in fact supervise the workers’ performance of their work in any way. Is the office park a joint employer of the janitorial employees?
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> Under these facts, the office park is not a joint employer of the janitorial employees because it does not hire or fire the employees, determine their rate or method of payment, or exercise control over their conditions of employment. The office park’s reserved contractual right to control the employee’s conditions of employment does not demonstrate that it is a joint employer.

The DOL’s inclusion of this example is significant to a PEO because under many state licensing laws and PEO client service agreements, the PEO must reserve the right to direct and control worksite employees (co-employees). Keep in mind, under state PEO laws, a PEO receives the right to do certain “employer” functions such as securing workers’ compensation insurance, reporting payroll for unemployment and payroll taxes, filing and withholding payroll taxes, and arguably the reservation of direction and/or control serves as a basis to grant such employer rights. At the same time, it is well known and accepted that a PEO

almost never actually exercises these rights. It is just not practical and not reflective of the reality of the relationship. The client continues to maintain control and direction over the worksite employees and workplace. Because the standard reservation of rights could potentially provide an opening to allege joint employer status, the DOL's inclusion of this example should help defeat such a claim.

This example makes clear the DOL's position that for purposes of wage and hour laws, reserving a right of direction of control without exercising that right is not a factor in considering whether joint employer status exists. This is good news for PEOs.

On the other hand, the proposed rule does present a potentially serious problem for PEOs. There is no requirement that more than one factor must be present. Thus, as written, the presence of just one factor could form the basis of a finding of joint employers. Reliance on one factor is very problematic for PEOs because every PEO maintains employee records of worksite employees, which is one of the four factors, and a PEO may be required to maintain such records under state or federal law. Despite the lack of any PEO specific example in the proposed rule, the DOL could nonetheless rely on this single factor to find a PEO a joint employer.

Risks to PEOs and Staffing Companies

Technically, the proposed joint employer rule applies only to wage and hour issues under the FLSA. Even with this relatively narrow application, the risk to a PEO of a finding of joint employer with its client is potentially enormous. As a "joint employer," a PEO could be held liable for a wage and hour violation committed by its client – without knowledge of the PEO, and even if a court was to agree that the PEO is not an employer under the FLSA. This is the primary direct risk of the proposed rule. However, there is case law favoring the PEO on this point. Wage and hour violations are typically not covered by Employment Practices Liability Insurance, so it can

be a costly holding. The risk of having to answer for a violation of a PEO client became more acute after considering the DOL's recently announced proposed rule that would make more than a million additional workers eligible for overtime under the "white collar" overtime exemptions under the Fair Labor Standards Act (FLSA). This proposed rule, published on March 7, 2019, would increase the standard salary level from $455 per week to $679 per week ($35,308 annually). Above this salary level, eligibility for overtime varies based on job duties. With the increased salary, however, the proposal permits employers to count non-discretionary bonuses and incentive payments (including commissions) paid on an annual or more-frequent basis to satisfy up to 10 percent of the standard salary level.

The proposal also changes the salary basis for highly compensated employees, which increases from $100,000 to $147,414 per year.

If a PEO is found to be a joint employer under the proposed joint employer rule, a PEO could be held jointly and severally liable for an overtime violation of its client.

For staffing agencies, the rule is more direct in its impact. One of the examples from the DOL specifically describes a typical staffing agency relationship and concludes the arrangement would constitute joint employer status between the agency and its client. Clients of staffing agencies will not be pleased with the prospect of joint employer status in every traditional staffing relationship and could seek alternative ways to supplement their workforce.

In the end, although the proposed rule appears to be a good start for PEOs by retreating from the more expansive view of joint employers, the proposed rule also presents serious risks depending on how the "one factor" weighting turns out. Stay tuned. For guidance, consult your Akerman Labor and Employment lawyer.