Who's The Boss? Defeating Joint Employment Allegations Early in Employment Litigation

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I. Introduction

It has become an increasingly common practice for plaintiffs to name multiple defendants in employment actions under a joint employer theory. Under this theory plaintiffs seek to hold the alleged employers jointly and severally liable for any statutory employment law violation, or other harm, caused in the course of such alleged employment. Joint employers may include other parties with whom the direct or primary employer has contracted to perform services such as delivery or distribution services. They may include subsidiaries or joint venturers of the direct employer. Such cases present unique litigation risks and are typically complicated and costly to defend.

Understanding the joint employment theory can lead to strategies for attacking the claims early in the litigation at the pleading stage. Plaintiffs' efforts to broaden their potential recovery sources by naming larger, but more attenuated entities are often based on legal conclusions rather than specific facts and frequently seek to expand the scope of this theory. In such cases the claims can be ripe for attack by a motion to dismiss under Federal Rule of Civil Procedure (FRCP) 12(b)(6), given more stringent pleading requirements articulated in recent Supreme Court decisions, or corresponding state court procedures.

II. Joint Employment Under Federal and California Law

Joint employment claims generally posit that two separate entities are both employers and thus jointly and severally liable for alleged statutory employment violations claimed by an individual or group of individuals during alleged employment status. These cases are often brought pursuant to the Fair Labor Standards Act, 29 U.S.C. § 201 *et seq.*, (the "FLSA") or state counterpart statutes claiming failure to pay overtime wages, minimum wages, or to provide meal and rest periods. However, such claims can also be brought in wrongful termination, harassment and discrimination actions, particularly in cases involving contract employees or independent contractors. Joint employment can arise in any situation where one business has retained another business to provide services using its own employees or contractors.

Federal jurisprudence has developed a relatively comprehensive analysis for identifying a joint employment relationship., while California decisions have recently provided more guidance. The California Supreme Court recently took a significant step toward clarifying the joint employment analysis, at least in wage and hour cases: *Martinez v. Combs*, 2010 Cal. LEXIS 4660 (Cal. May 20, 2010). The *Martinez* decision provides further insight about how to defeat California joint employment claims in business relationships involving several contracting parties.

(a) Federal Joint Employment Law

The federal courts have devised various legal tests to determine joint employment status. These tests are similar but vary with the circumstances and tend towards specific multi-factor tests. In the Ninth Circuit, the primary test for joint employment under the FLSA is a four-factor "economic reality" test articulated in *Bonnette v. Cal. Health & Welfare Agency*, 704 F.2d 1465, 1470 (9th Cir. 1983).[1] The test queries whether the alleged employer: (1) had the power to hire and fire employees, (2) supervised and controlled employee work schedules or conditions of employment, (3) determined the rate and method of payment, and (4) maintained employment records. The Ninth Circuit developed this test in light of the Supreme Court's statement that the "economic reality" rather than "technical concepts" is the employment test, and because the FLSA's definition of employer is to be interpreted broadly and liberally: *Goldberg v. Whitaker House Coop., Inc.*, 366 U.S. 28, 33 (1961).[2]

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While these four factors have been generally adopted throughout the Federal circuits, some courts have expanded and modified these factors for application to specific case circumstances.[3] For example, in *Tumulty v. FedEx Ground Package System, Inc.* the District Court found that FedEx was a joint employer of the plaintiff drivers who worked for independent contractors that contracted to deliver packages for FedEx: 2005 U.S. Dist. LEXIS 26215 (W.D. Wash. March 7, 2005). The *Tumulty* court relied on the four *Bonnette* factors, but also considered an additional eight factors adapted by the Ninth Circuit from other FLSA cases in *Torres-Lopez v. May*, 111 F. 3d 633 (9th Cir. 1997).

In *Tumulty*, the plaintiffs filed a lawsuit seeking damages for unpaid overtime and wrongful termination against both FedEx and the independent contractors who directly employed them. Facts that the court found decisive in determining that there was joint employment included the finding that FedEx could fire drivers hired by the independent contractor; that it supervised and controlled drivers' conditions of employment by holding weekly meetings; commented on drivers' uniforms and checked on the delivery of packages by drivers; and that FedEx maintained records on the drivers that qualified as "employment records." Further, drivers were required to contact FedEx managers if they could not deliver packages. FedEx would also assign extra work, order the drivers to drive other routes, and suggest the number of hours drivers should be on the road each day – all further indicia of employment status. The court also found it significant that the nature of the drivers' work was routine and they relied heavily on FedEx's terminal facilities to perform their work: *Tumulty*, U.S. Dist. LEXIS 26215 at 8-11.[4]

(b) California Joint Employment Law

California courts have drawn on many of the same factors employed by the federal courts, but have generally agreed that there is no set test or list of dispositive factors. Instead, courts analyze the "myriad facts surrounding the employment relationship in question": *Vernon v. State of California*, 116 Cal. App. 4th 114, 124-25 (Cal. 2004). The approach to the joint employment question in California has been based on the different statutory frameworks from which employment claims arise. For example, the California Fair Employment and Housing Act ("FEHA"), California's anti-discrimination statute,[5] provides only a nominal "employer" definition stating in part: "Employer includes any person regularly employing five or more persons, or any person acting as an agent of an employer, directly or indirectly....": *Vernon, supra*, 116 Cal. App.4th at 124, citing Cal. Gov't Code § 12926(d). At pp. 124-126 the *Vernon* court (analyzing a FEHA claim) noted that courts place most emphasis on the control over employment conditions, observing that in all cases in which an employment relationship is found, that an employer is an entity that extends a significant degree of control over the plaintiff.

Vernon is notable as involving a successful motion to dismiss joint employment allegations.[6] The trial court sustained the State of California's demurrer[7] on the grounds the state was not the plaintiff's joint employer as a matter of law. While emphasizing the importance of control, the Court of Appeal found it particularly compelling that the alleged state employer did not pay the plaintiff for his services either directly or indirectly. The court noted that while this factor was not controlling, "the absence of any direct or indirect remuneration from the defendant to the plaintiff...is at least strong evidence that an employment relationship did not exist": *Vernon*, 116 Cal. App. 4th at 126.

There has been little specific California authority on what "employ" or "employer" means in wage and hour claims until recently. In 2006, a federal district court applied the FLSA's joint employer test to California wage and hour claims because of the "similarity between the FLSA and the California [wage and hour] laws at issue": *Rios v. Airborne Express, Inc.*, 2006 U.S. Dist. LEXIS 54570, *4 (N.D. Cal. July 24, 2006). The Court further noted that "California courts do not appear explicitly to have created a joint employer test" for wage and hour claims.[8]

The California Supreme Court's recent *Martinez* decision clarified when an entity, or multiple entities, jointly or individually "employ" workers for purposes of California wage cases that arise under California Labor Code section 1194 (hereafter "Section 1194"). Section 1194 provides a civil cause of action to employees who receive less than the legal minimum wage or the legal overtime compensation. The plaintiffs were agricultural workers and brought suit alleging violations of California wage and hour laws. They alleged that their employers included not only the direct farm operator employer, but they also sought to extend liability to produce distributors with whom their direct employer contracted to sell goods. The Court refused to extend liability this far.

The court articulated a California-specific test based on Section 1194, rejecting federal tests. The court held unequivocally that, in interpreting the definition of "employer" under Section 1194, the IWC wage orders control.[9] In the IWC wage orders, "'employ' means to engage, suffer, or permit to work," and "employer" means any person as defined in Section 18 of the California Labor Code, who directly or indirectly, or through an agent or any other person, employs or exercises control over the wages, hours, or working conditions of any person."[10] The court concluded that the IWC wage orders provide three alternative definitions of employ, recognizing that the common law definition for "employ" is merely one alternative stating: "[To employ] means: (a) to exercise control over the

wages, hours or working conditions, or (b) to suffer or permit to work, or (c) to engage, thereby creating a common law employment relationship."[11]

The *Martinez* Court found that the defendants were not the plaintiffs' joint employers. Plaintiffs argued that the defendant producer distributors Apio and Combs "suffered or permitted" plaintiffs to work because they knew plaintiffs were working and benefited from the work they performed.[12] This went too far. The Court found that "the concept of a benefit is neither a necessary nor a sufficient condition for liability under the 'suffer or permit' standard."[13] Instead, the standard is whether the defendant has knowledge of and fails to prevent the work from occurring. Here, the direct employer Munoz had the exclusive power to hire and fire his workers and the distributors Apio and Combs did not have the power to prevent plaintiffs from working.[14] The Court also rejected the asserted "benefit" theory as imposing "potentially endless chains of liability"[15] thereby potentially extending liability through the distribution chain to grocers and even consumers. Importantly, the Court attempted to draw a bright line for contracting parties in integrated business relationships that would allow them to minimize their risk of joint and several liability for employee wage claims.

Plaintiffs also claimed that distributor Apio dominated Munoz's business financially and therefore exercised indirect control over his employees' wages and hours. The Court rejected this argument too, noting that only Munoz had control over plaintiffs' wages, hours and working conditions.[16] Munoz alone hired and fired plaintiffs, trained and supervised them, determined their rate and manner of pay, and set their hours and work locations.[17] Further, Munoz operated "a single, integrated business operation" that grew and harvested produce for several unrelated merchants "*in the hope of earning a profit at the end of the season.*" (emphasis added)[18] The Court emphasized that Munoz was not Apio's employee and that Munoz "enjoyed an opportunity for profit."[19] This emphasis on profit echoes a recent case upholding independent contractor status. *See FedEx Home Delivery v. NLRB*, 563 F.3d 492 (D.C. Cir. 2009). In *FedEx Home Delivery*, the D.C. Circuit noted that an important animating principle in evaluating whether persons were independent contractors is whether "the position presents the opportunities and risks inherent in entrepreneurialism."[20]

The *Martinez* plaintiffs also argued that defendant produce distributors exercised significant control over their working conditions because defendants' representatives were frequently in the fields evaluating the quality of the produce the workers were harvesting and observing them work. These representatives would even from time to time direct the workers on how to pick and package the produce. The Court again rejected the argument, noting that Munoz's employees never viewed the field representatives as their supervisors and only Munoz had the right to exercise control over the manner in which they worked.[21]

III. Attacking Joint Employment Claims at the Pleading Stage

Defending complex employment cases where multiple defendants are alleged to be joint employers is costly and poses increased litigation risks for the defendants. Given the highly factual analysis, defeating joint employment allegations and successfully obtaining dismissal of inappropriate defendants short of trial can be difficult. Indeed, it is usually delayed until summary judgment late in the case after extensive and costly discovery.

Nonetheless, under certain circumstances, joint employment allegations may be susceptible to attack at the pleading stage through a motion to dismiss under FRCP 12(b)(6) or similar state court procedure. In *Ashcroft v. Iqbal*, 129 S.Ct. 1937 (2009) the Supreme Court overruled the liberal pleading standard articulated over 50 years ago in *Conley v. Gibson*, 355 U.S. 41 (1957). *Iqbal* expanded the "plausibility" standard first introduced in *Bell Atlantic v. Twombly*, 550 U.S. 544, 570 (2007). A claim is "plausible" when facts are pled that allow the court to draw "the reasonable inference that the defendant is liable for the misconduct alleged": *Iqbal*, 129 S.Ct. at 1949. Under this "plausibility" standard, the factual allegations in a complaint must be more than "labels and conclusions," and instead must raise the right to relief to a more than speculative level: *Twombly*, 550 U.S. at 555. Together *Iqbal* and *Twombly* represent a significant change in federal pleading requirements.

Iqbal sets an explicit two-step analysis for adjudicating motions to dismiss in federal cases. First, a court must identify and reject any legal conclusions that are unsupported by factual allegations because they are "not entitled to the assumption of truth." *Iqbal*, 129 S.Ct. at 1949-1950 ("Threadbare recitals ... supported by mere conclusory statements" are insufficient to survive a motion to dismiss.) Second, a court must conduct a "context-specific" analysis that "draw[s] on [the court's] experience and common sense" to determine whether the allegations "plausibly give rise to an entitlement to relief."[22] In sum, to survive a motion to dismiss under the current federal pleading standard, the complaint must present a story "plausible" enough to convince a judge that the plaintiff actually stands a reasonable chance of proving the complaint claims. *Iqbal*, 129 S.Ct. at 1949.

Iqbal has particular import in joint employment cases because it is common for plaintiffs to claim each entity in a distribution chain is an employee and to do so in conclusory fashion. Defendants can frequently argue with force that such joint employment allegations, with few specific facts so as to

demonstrate the indicia of employment are insufficient. Such motions can be buttressed by introducing facts subject to judicial notice and thus available for consideration by the court.

For example, a plaintiff in a wage and hour class action may choose not to name as a defendant the independent contractor who directly employs them, in hopes that they can later bring the independent contractors in as putative class members. Instead, the plaintiff names as joint employers the companies for whom the independent contractor performs delivery services. The failure to name the entity that directly employed and paid the plaintiff is subject to attack as a failure to meet the "plausibility" test outlined in *Iqbal*. In *Vernon*, *supra*, the plaintiff failed to allege sufficient facts to demonstrate joint employment status. Although not dispositive, the Court found as significant the fact that the State did not pay any compensation to the plaintiff: *Vernon*, 116 Cal. App. 4th at 126. The Court noted while the actual payment of wages is not dispositive, it can be a key factor in the joint employment analysis. *Vernon* can be used to attack putative class action claims under joint employment theory in California where some of the defendants neither actually paid the plaintiff employees nor directly participated in setting their pay.

The California Supreme Court's *Martinez* decision also recognized the importance of evaluating "exercise of control" over working conditions, a factor that was critical in *Vernon*. *Martinez* also considered the pay setting factor. While *Martinez* recognizes a broad definition for "employ" and "employer" as promulgated by the IWC, the Supreme Court also signaled a willingness to set limits to joint employment based or direct control. The Court's careful analysis and rejection of a purported joint employment relationship involving several downstream contracting entities supports imposing limits on this expansive employment theory.

As such, an aggressive strategy of an early attack under a joint employment cause of action will generally be sound and cost effective. While a motion to dismiss may result in an amended complaint, it also increases the litigation risk for plaintiffs and offers a mechanism to promptly attack claims that have little factual support and/or seek to expand the scope of alleged joint employment to defendants further down the distribution chain. An early motion can be a very effective strategy to obtain dismissal of some defendants or narrow the claims, a result that not only may limit case value but serves to educate the court on weaknesses on plaintiff's claim. Such motions tend to be cost-effective and can narrow discovery and increase the likelihood of favorable early settlement.

Although in class action cases a successful motion has no *res judicata* effect on future claims brought by putative class members prior to class certification and applies only to the named plaintiff or plaintiffs, there can be no doubt that such a ruling can have a deterrent effect to future actions in addition to bringing the instant case to a close. Given the heightened pleading standard in federal court, in particular, this strategy should be considered in all high stakes complex employment litigation where joint employment is alleged.

IV. Conclusion

When faced with a joint employment case, counsel should carefully consider bringing an early motion to dismiss. Doing so can streamline the case by potentially eliminating defendants, certain specific claims, and reducing the case value from the plaintiff's perspective.

Endnotes

1. Disapproved on other grounds in *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528 (1985).
2. The Department of Labor has promulgated joint employment regulations applicable to the FLSA at 29 C.F.R. 791.2
3. *See Zheng v. Liberty Apparel Co., Inc.*, 355 F.3d 61 (2d Cir. 2003) [utilizing six factors developed using the *Bonnette* analysis].
4. District courts in other circuits have considered similar joint employment arguments in the transportation industry and have analyzed alleged joint employment status under multi-factor tests unique to the given circuit and the statutes under which the claims were alleged. *See, Vega v. Contract Cleaning Maintenance, Inc.; United Parcel Service; et al.*, 2004 U.S. Dist. LEXIS 20949, *19-20 (N.D. Ill. October 18, 2004). The court rejected the 9th Circuit's Bonnette factors in favor of those used by the 2d Circuit, and found that UPS could be a joint employer because, even though it did not hire, fire or pay Contract Cleaning Maintenance, Inc.'s ("CCM") employees, CCM's employees worked on UPS premises, UPS set their work hours, gave detailed work assignments, supervised their work and maintained records of hours worked. See also *Lemmings v. FedEx Ground Package System, Inc.*, 492 F.Supp.2d 880, *17 (W.D. T.N. May 15, 2007) [In a sexual harassment case, the court applied the 6th Circuit's "common law test of agency" as opposed to the "economic reality test" and, analyzing the right to control, determined that FedEx was not a joint employer because FedEx did not retain any influence over the terms and conditions of the plaintiff's employment by her direct employer.].
5. California Government Code § 12940, et seq.
6. While the case facts were unique, the decision is an example of a successful attack on the joint employment theory at the pleading stage. The plaintiff was a former firefighter for the City of Berkeley, who had a skin condition that prevented him from shaving his beard. Firefighters are often required to use a special type of respirator in their fire suppression efforts. The State of California, through Cal-OSHA, adopted regulations that prevented anyone from using such a respirator who had facial hair. The plaintiff sued the State of California, alleging racial discrimination under the FEHA, a statute which is typically reserved for claims against employers.

7. A Demurrer is the procedural equivalent for FRCP 12(b)(6) motion in federal court under California practice.
8. *Id.*
9. *Id* at 25. Although Martinez is limited to actions arising out of Section 1194, governing payment of minimum wages and overtime compensation, it is likely this case will also control in cases raising other California wage and hour claims, such as meal and rest period violations.
10. *See, e.g.*, Cal. Code Regs. tit. 8, § 11090, subd. 2(D), (F).
11. *Id.* at 57.
12. *Id.* at 69.
13. *Id.* at 70.
14. *Id.*
15. *Id.* at 72.
16. *Id.* at 74.
17. *Id.* at 76-77.
18. *Id.* at 76.
19. *Id.* at 79.
21. *Id.* at 86-87
22. *Id.* at 1950-1951 (the "mere possibility" of misconduct is insufficient). See also: *Harris v. Amgen, Inc.*, 573 F.3d 728 (9th Cir. 2009) and *Tibble v. Edison International*, et al., 2009 U.S. Dist. LEXIS 67752 (C.D. Cal. July 31, 2009), (complaint dismissed because "conclusory statement did not identify any specific transactions").