SUTHERLAND

LEGAL ALERT

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Hire Unpaid Interns at Your Peril

While Vince Vaughn and Owen Wilson have recently brought some attention to the internship position by comically portraying the life of Google interns in the movie *The Internship*, the U.S. District Court for the Southern District of New York has issued an important decision that provides guidance to employers on when their unpaid interns will be considered "employees" for purposes of federal and state labor laws. *Glatt, et al. v. Fox Searchlight Pictures Inc.*, Case 11 Civ. 8784 (WHP) (S.D.N.Y. June 11, 2013). The *Fox* decision adopts a broad definition of an "employee" that is likely to include many unpaid interns and a narrow interpretation of the "trainee" exception that was previously recognized by the U.S. Supreme Court. The decision may well result in a significant increase of lawsuits against employers that use or have used unpaid interns and a sharp reduction in companies using unpaid interns.

Ironically, the unpaid interns in the *Fox* case were working in the movie industry. Two of the plaintiffs, Footman and Glatt, contended that the defendant violated federal and state laws by classifying them as unpaid interns instead of paid employees. Footman and Glatt each worked on production of the film, *Black Swan,* in New York. After production, Glatt took a second unpaid internship relating to *Black Swan's* post-production. As discussed below, the *Fox* court held that they were improperly classified and should have been classified as employees. The *Fox* court also granted a motion for class certification of another plaintiff intern's New York Labor Law (NYLL) claims against the defendant pursuant to Federal Rule of Civil Procedure 23 and conditional certification of her Fair Labor Standards Act (FLSA) claims. As this decision shows, employers need to be very careful in hiring persons as unpaid interns because this may put them at risk for FLSA and/or state labor law claims arising from misclassifications.

Employees vs. Trainees

In *Fox,* Judge William H. Pauley, III granted the two interns' summary judgment with respect to their contention that they were "employees" covered by the FLSA and NYLL. In so ruling, the court rejected the employer defendant's contentions that they fell under the "trainee" exception established by the U.S. Supreme Court in *Walling v. Portland Terminal Co.*, 330 U.S. 148 (1947). The *Fox* court found that the *Walling* court's decision was premised on the fact that the railroad employer involved received "no immediate advantage" from any work done by the trainees. The Supreme Court in *Walling* reasoned that the FLSA was not intended to penalize employers for providing at no cost the same type of training one could get at a vocational school. The *Fox* court found that the employer in the instant case received clear benefits from the labor supplied by plaintiffs and, therefore, the narrow *Walling* "trainee" exception was inapplicable.

In reaching this decision, Judge Pauley also rejected the "primary beneficiary" test that has been employed by some other courts which focuses the employee classification decision on a factual determination of whether the intern or his or her employer was the "primary beneficiary" of the intern's labor. If the employer was the "primary beneficiary," then the intern is an employee. If the intern was the primary beneficiary, then the intern is not considered an employee. The "primary beneficiary" test has been employed by the U.S. Court of Appeals for Fourth and Sixth Circuits, but Judge Pauley found it to be inconsistent with *Walling.*

Analysis Pursuant to the Six DOL Factors

Rather than adopting the "primary beneficiary" test, Judge Pauley endorsed using Department of Labor (DOL) Fact Sheet #71 as a basis for ascertaining whether an intern at a for-profit company falls within the narrow "trainee" exception recognized by *Walling*. The DOL has identified the following criteria that should be considered in this analysis:

1. 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;
2. The internship experience is for the benefit of the intern;
3. The intern does not displace regular employees, but works under close supervision of existing staff;
4. 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;
5. The intern is not necessarily entitled to a job at the conclusion of the internship; and
6. The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship.

The *Fox* court found that each of these DOL factors found support in *Walling.*[1]

In *Fox,* Judge Pauley analyzed the six DOL factors for the two plaintiffs. Looking at the first DOL factor, he found that Footman did not receive any formal training or education during his internship. The court found that it was not enough that Footman learned about the function of a production office by being there just as other paid employees were. Judge Pauley found that the record was inconclusive for Glatt on this factor noting that Glatt's testimony that "he didn't learn much" did not establish that he did not, in fact, receive training from his employer.

With respect to the second DOL factor, whether the experience is for the benefit of the intern, Judge Pauley found that although the interns did receive some benefits from their internships such as resume listings, references and knowledge of how a production office works, these benefits were the same benefits that any paid employee working in the office would receive. In contrast, the court found that the employer received the benefits of the interns' unpaid work which it otherwise would have had paid employees perform. Judge Pauley found that as a result, even if the more employer friendly "primary beneficiary" test were employed, the interns still should have been classified as employees rather than interns because the employer was the primary beneficiary of the interns' labor.

Judge Pauley found that the third DOL factor, displacement of regular employees, also supported the interns being employees because the evidence established that the routine tasks they performed would have to be performed by either other existing paid employees working longer hours or by bringing in additional paid staff. In analyzing the fourth DOL factor, the *Fox* court found that the employer obtained an immediate benefit from the two interns' work even though much of the work was menial. The *Fox* court noted that there was no evidence that the interns impeded work, and the fact that they were beginners and might be less efficient, did not affect that they were employees. With respect to the fifth DOL factor, Judge Pauley found that there was no evidence that either intern was entitled to a job at the end of the internships or thought that there would be jobs available. Finally, with respect to the sixth DOL factor, while the court found that both interns understood they would not be paid, the court attached little

[1] The *Glatt* court also rejected that the April 2010 release of DOL Fact Sheet #71 constituted a change in the law finding that the six factors were consistent with *Walling* and had appeared in Wage and Hour Administrator opinions since 1967.

significance to this factor, noting that the FLSA does not allow employees to waive their entitlement to wages.

Looking at the totality of the circumstances, the *Fox* court found that the plaintiffs were "employees" covered by the FLSA and NYLLs and that they had been improperly classified as "interns" by the defendants.

Certification of the NYLL and FLSA Intern Claims

The *Fox* court also granted the motions of another plaintiff to (a) certify a class pursuant to Federal Rule of Civil Procedure 23 consisting of all individuals who had unpaid internships in New York with the Fox defendant and related entities for purposes of litigating her NYLL claims and (b) conditionally certify a class with respect to her FLSA claims.

Analyzing the Rule 23 motion based on *Wal-Mart Stores, Inc. v. Dukes*, 131 S.Ct. 2541, 2548 (2011), the *Fox* court found the Rule 23 requirements of numerosity, commonality, typicality, predominance and superiority were all met. Judge Pauley found that there were at least 40 interns that would be part of the class and that this number was sufficient to meet the numerosity requirement. The *Fox* court found commonality because the plaintiff had identified evidence capable of answering common questions on a classwide basis. Specifically, the court recognized that there was evidence that (a) departments at the defendant Fox companies requested interns based on "need" and requested more unpaid interns when they were busier, which is the opposite of what would be expected to occur if the interns provided little advantage or impeded work; (b) more unpaid interns were added when paid internships were eliminated and overtime and temporary employees were reduced; and (c) after the DOL factors were released in 2010, a supervisor asked an intern recruiter "why would an office have an intern that provides no immediate advantage from said intern's activities," and some changes were contemplated and/or made at the defendant companies in response to the release of the DOL factors. Judge Pauley found this was evidence capable of generating common answers to questions of liability on plaintiff's NYLL claims.

The court found the plaintiff met the typicality requirement because she had participated in the same internship program administered by the same recruiters and was classified as an unpaid class member like other class members claiming violations of the NYLLs. Judge Pauley found her to be an adequate class plaintiff because her claims were typical of the class and her counsel was experienced in prosecuting these types of cases.

The Aftermath of the *Fox* Decision

Employers need to think long and hard before bringing in unpaid interns. If the purpose is to help meet the employer's workload, the intern should be paid. DOL Fact Sheet #71 provides guidance and parameters for determining when an intern may be unpaid. These factors should be reviewed if the company employs unpaid interns or is considering doing so. In addition, employers should consult and be familiar with applicable state labor laws. In light of the *Fox* decision, there may be a rise in FLSA and state law claims relating to this issue, and many of these claims may be brought as class or collective actions. Indeed, yesterday, a former intern filed a class action lawsuit in the Supreme Court of New York against Warner Music Group and Atlantic Records claiming violations of the New York Labor Laws including failure to pay minimum wages, overtime compensation and any wages.

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If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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