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INTERNS

Several high-profile lawsuits recently have been filed challenging the legality of unpaid internships, Dechert LLP attorney Jeffrey W. Rubin says in this BNA Insights article. He discusses the multiple elements of the test developed by the Labor Department's Wage and Hour Division to determine whether individual interns or trainees are ''employees'' for purposes of the Fair Labor Standards Act and warns that all the criteria must be met to establish a nonemployment relationship.

Although there currently is a ''dearth'' of judicial precedent regarding unpaid internships, a situation that may soon change due to the pending lawsuits, Rubin examines court rulings involving the analogous situation of trainees and finds they have taken a variety of approaches. Finally, he offers precautions employers can take in structuring their internship programs so they comply with the FLSA.

Risky Business: Using Unpaid Interns

By Jeffrey W. Rubin and Michael Berkowitz

Employer use of unpaid internships has increased substantially in recent years. In lieu of pay, employers may offer internships that provide a wealth of experience and knowledge that interns can then use as a resume builder or even as a gateway into the marketplace.

A number of high-profile lawsuits, however, have recently been filed challenging these unpaid internship arrangements as unlawful. The plaintiffs in these lawsuits allege that they were misclassified as ''unpaid interns'' to circumvent wage-and-hour laws. Employers can significantly reduce the risk of litigation by properly structuring their unpaid internship programs.

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The Legal Landscape

The Fair Labor Standards Act is the federal wage-and-hour law of general application. It requires that all employees working in covered activities be paid at least a specified minimum wage and receive overtime pay for hours worked in excess of 40 hours per week. Section 206(a)(1) of the FLSA sets the current federal minimum wage at $7.25 per hour, and Section 207(a)(1) requires overtime pay at a minimum of one and a half times the employee's regular rate, unless the employee fits into one or more of the enumerated exceptions.

There is no exception under the FLSA for ''interns.'' Rather, the recent suits focus on the definition of the term ''employee'' under the FLSA and whether interns fit that definition. The FLSA defines ''employee'' as ''any individual employed by an employer,'' defines ''employer'' to include ''any person acting directly or indirectly in the interest of an employer in relation to an employee,'' and defines the term ''employ'' to include ''to suffer or permit to work.'' 29 U.S.C. § 203. These

circular definitions provide no helpful guidance to employers attempting to comply with the FLSA's requirements. Instead, it has been left to the courts and the Department of Labor, the agency charged with administering the FLSA, to interpret these terms.

The U.S. Supreme Court addressed these broad terms in *Walling v. Portland Terminal Co.*, 330 U.S. 148 (1947), where the court was asked to determine whether trainees were covered by the FLSA. In holding that they were not, the court recognized that while broad in scope, the term ''employee'' in the FLSA ''cannot be interpreted so as to make a person whose work serves only his own interest an employee of another person who gives him aid and instruction.'' Id. at 152. In its majority opinion, the Supreme Court stated that an employer should derive no ''immediate advantage'' from a trainee and should not use the training to ''violate either the letter or spirit of the minimum wage law.'' Id. at 153.

From this ruling, DOL's Wage and Hour Division and the courts have created tests to determine whether individuals are trainees/interns or ''employees'' for purposes of the FLSA.

WHD's Test for Unpaid Interns

Based on *Walling*, WHD established a six-factor test to determine whether an individual is an intern or trainee for purposes of the FLSA. WHD has applied this test for decades in its opinion letters and published a fact sheet devoted to this topic approximately two years ago (77 DLR A-3, 4/23/10). According to DOL's Fact Sheet #71, the following six criteria must be applied when determining if an internship program is properly excluded from the wage requirements of the FLSA:

1. The internship, even though it includes actual operation of the facilities of the employer, is similar to training that 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 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.
6. The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship.

If all six of these factors are met, DOL will conclude that an employment relationship does not exist under the FLSA, and the FLSA's minimum wage and overtime provisions do not apply to the intern. Id.

To satisfy the first factor of the test—that the internship is similar to the training in an educational environment—WHD provides that ''the more an internship program is structured around a classroom or academic experience as opposed to the employer's actual operations, the more likely the internship will be viewed as an extension of the individual's educational experience.'' Id. Factors to consider include the similarity of the internship program to the curriculum in a vocational school, whether or not the skill sets acquired are transferable between different employers within the given industry, and whether or not a college or university oversees the internship program or provides education credit. This last factor has led many employers to restrict their internship program to students who will receive academic credit for their participation.

The determination of whether the intern is the primary beneficiary under the second factor of the test often involves a comparative analysis of the benefits to the intern and the would-be employer. An intern almost always receives some benefit from an internship, whether in the form of exposure to certain industries or connections with certain individuals. Showing that criteria 1 and 4 are met helps to establish that the intern is the primary beneficiary of the internship. If an internship provides a bona fide educational experience, it is more likely that the intern is the primary beneficiary. Also, if the employer derives no immediate advantage from the activities of the intern, it is more likely the intern is the primary beneficiary.

The third factor of the WHD test requires both that the intern not displace regular employees of the employer and that the intern works under the close supervision of existing employees. On the former criterion, WHD takes the position that if the employer would have to increase current employee workloads or hire new employees had the internship not been created, even if only for seasonal or peak times, the interns will be considered employees. The same is true if the employer uses the interns to substitute for absent regular employees. With respect to the supervision prong, both absolute and relative supervision are of importance. The more supervision an intern receives, the more likely the internship is a bona fide educational experience. However, if an intern receives the same amount of supervision as a regular employee, this fact would suggest an employment relationship. Employers that satisfy this criterion often have the intern or trainee spend the majority of their time shadowing and observing regular employees.

To satisfy the fourth criterion of the WHD test, that the employer derives no immediate advantage from the activities of the intern and its operations may occasionally be hindered, the intern should not ''perform the routine work of the business on a regular and recurring basis, and the business [should not be] dependent upon the work of the intern.'' Id. The showing required to satisfy criteria 2, 3, and 4 are often interrelated, and showing that criteria 2 and 3 are met helps to establish that criterion 4 is satisfied.

Under WHD's test, the intern must not be guaranteed a job upon completion of the internship under criteria 5. Rather, the internship should be for a duration fixed prior to the outset of the program. Employers should not use unpaid internships as a ''trial period'' for potential future employees. WHD views interns or trainees in programs of this type to be employees under the FLSA.

Finally, a critical element to any unpaid internship program, and the sixth requirement of the WHD test, is that both the intern and the would-be employer understand that the internship is unpaid. This understanding should preferably be set forth in a writing signed by the intern prior to the start of the internship. WHD has recognized, however, that interns can be provided with a stipend without creating an employment relationship if the stipend ''does not exceed the reasonable approximation of the expenses incurred by the interns involved in the program.'' Opinion Letter (May 8, 1996).

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The WHD test is fairly rigid and difficult to meet for most modern internship programs, especially given the requirement that the employer derive no immediate benefit from the intern's work. Most employers view internships as mutually beneficial, and commentators have urged WHD to modify its test accordingly. Despite these calls, DOL has not modified its test and has recently increased its efforts to curb what it views as abuses of the FLSA, including through unpaid internship programs. Nancy J. Leppink, deputy wage and hour administrator of WHD and acting wage and hour administrator since January 2011, commented that ''[i]f you're a for-profit employer or you want to pursue an internship with a for-profit employer, there aren't going to be many circumstances where you can have an internship and not be paid and still be in compliance with the law.'' Steven Greenhouse, *The Unpaid Intern, Legal or Not*, N.Y. Times, Apr. 2, 2010.

Judicial Interpretation of WHD's Test and the Requirements for Bona Fide Unpaid Internships

There is currently a dearth of judicial precedent regarding unpaid internships, although that may quickly change given the number of recently filed suits challenging the practice. There is judicial precedent, however, involving the analogous situation of trainees. The Supreme Court's decision in *Walling* involved trainees, and WHD's test for internships, which it also applies to training programs, was based on *Walling*.

DOL's WHD test for interns is rigid. That is, all six criteria must be met in order to establish a nonemployment relationship. Since the test is not contained in formal modes of agency communication, such as notice-and-comment rulemaking, courts are not required to adhere to WHD's test wholesale. Rather, courts must only follow the test to the extent it is persuasive. Not surprisingly, the court cases to have addressed the issue in the context of trainees have not been uniform in their adoption of the WHD test or the specific test to apply.

By way of example, in *Reich v. Parker Fire Protection District*, 992 F.2d 1023, 1 WH Cases2d 748 (10th Cir. 1993), the U.S. Court of Appeals for the Tenth Circuit determined that a totality-of-the-circumstances approach should be applied to determine whether individuals are trainees or employees under the FLSA. *Reich* involved the requirement of Parker Fire Protection District that any individual who wanted to become a firefighter in the district had to complete a 10-week, unpaid firefighting academy offered by the district. Because the district sent only the number of firefighters that it expected to hire to the academy, each individual had ''every reasonable expectation'' of being hired upon successful completion. The academy curriculum consisted of classroom lectures, tours of the district, demonstrations, physical training, and simulations. Toward the end of the training period, the trainees maintained certain training equipment and manned a truck, but were supervised while doing so. The trainees did not substitute for regular employees.

In applying WHD's six-factor test, the court concluded that each factor was satisfied except that each individual expected to, and was, hired following successful completion of the firefighting academy. Consistent with its totality-of-the circumstances approach, however, the Tenth Circuit held that the trainees were not employees for purposes of the FLSA because ''that single factor cannot carry the entire weight of an inquiry into the totality of the circumstances.'' Id. at 1029. Had the Tenth Circuit applied WHD's test strictly, it would have concluded instead that the trainees were ''employees'' under the FLSA and entitled to be compensated in accordance with its wage requirements.

The U.S. District Court for the Eastern District of Pennsylvania has applied a similar totality-of-the-circumstances test in determining whether an apprentice pilot was an employee entitled to wages under the FLSA. See *Bailey v. Pilots' Ass'n for Bay & River Del.*, 406 F. Supp. 1302, 22 WH Cases 723 (E.D. Pa. 1976). *Bailey* involved an apprentice pilot who performed the same work as regular pilots under minimal supervision and sometimes substituted for hired employees. Although the apprentice did not expect full compensation, the court concluded that the apprentice was an employee under the FLSA. Then-judge (now Supreme Court Justice) Sotomayor similarly applied a totality-of-the-circumstances approach in *Archie v. Grand Central Partnership Inc.*, 997 F. Supp. 504, 4 WH Cases2d 783 (S.D.N.Y. 1998).

Contrary to these courts, the Fourth and Sixth circuits have rejected the WHD test. In *Solis v. Laurelbrook Sanitarium & School*, 642 F.3d 518, 17 WH Cases2d 929 (6th Cir. 2011) (82 DLR AA-1, 4/28/11), in which the Sixth Circuit considered whether students were employees under the FLSA, the Sixth Circuit noted that ''[c]ourts differ on whether the WHD's test is entitled to controlling weight in determining employee status in a training context,'' and concluded that a focus ''on which party receives the primary benefit of the work performed'' is ''the appropriate inquiry.'' The Fourth Circuit also held in *McLaughlin v. Ensley*, 877 F.2d 1207, 29 WH Cases 537 (4th Cir. 1989), that ''the general test used to determine if an employee is entitled to the protections of the [FLSA] is whether the employee or the employer is the primary beneficiary of the trainees' labor.''

The trend of most courts to have considered the issue is to not adopt WHD's approach wholesale but to consider which party is the primary beneficiary of the arrangement or to look at all the relevant circumstances, including the factors in WHD's test. As a result, the outcome to be reached in certain cases may well depend on which governmental authority is making the determination.

Current Intern Lawsuits

As internships have become more prevalent, WHD was spurred into issuing its fact sheet two years ago, which sets forth for the public the WHD's long-standing test for determining whether interns or trainees are employees for purposes of the FLSA. The increasing use of interns will also require courts to address the issue as cases are brought by unpaid interns seeking to be paid for their efforts. A number of recent cases have been filed against employers by interns, especially in the media industry.

On Feb. 1, Xuedan Wang filed a class action suit against The Hearst Corp. claiming violations of the FLSA and related state law (23 DLR A-1, 2/3/12). See First Amended Class Action Complaint, *Wang v. Hearst Corp.*, No. 12-0793 (S.D.N.Y. Mar. 23, 2012). According

to the complaint, Wang was an unpaid ''Head Accessories Intern'' at *Harper's Bazaar*, a Hearst publication, from approximately August 2011 through December 2011. Wang's work was supervised by *Harper's Bazaar* staff and editors, and her job responsibilities as an unpaid intern included coordinating pickups and deliveries of samples between *Harper's Bazaar* and outside vendors, showrooms, and public relations firms; assigning unpaid interns to carry out scheduled pickups and deliveries; maintaining records relating to the magazine's sample trunks and fashion closet; providing onsite assistance at magazine photo shoots; managing corporate expense reports; and processing reimbursement requests. Wang alleged that Hearst benefitted from Wang's activities and that it would have hired additional employees or required existing staff to work additional hours without the assistance of Wang and other interns. Wang claimed that she should have been classified as an employee rather than an intern and thus paid for her work. Wang filed suit on behalf of herself and all other similarly situated interns, a potential class of more than 100 individuals. In July, the court denied Hearst's motion to strike the class and collective allegations under the FLSA and state law, and granted Plaintiff's cross-motion for conditional certification under the FLSA. See *Wang v. Hearst Corp.*, No. 12-0793, 2012 BL 175591 (S.D.N.Y. July 12, 2012) (135 DLR A-1, 7/13/12).

In another recent case, Fox Searchlight Pictures was sued by two former interns who worked for several months on the successful film *Black Swan*. See Class Action Complaint, *Glatt v. Fox Searchlight Pictures Inc.*, No. 11-6784 (S.D.N.Y. Sept. 28, 2011) (190 DLR A-1, 9/30/11). The lawsuit alleges that Fox Searchlight ''has been able to reduce its film production costs by employing a steady stream of unpaid interns'' and that these unpaid interns perform ''secretarial and janitorial work.'' In fact, one named plaintiff alleged that his responsibilities included preparing and maintaining coffee for the production office, taking and distributing lunch orders, taking out the trash, and cleaning the office.

A similar class action suit was filed in March against Charles Rose and Charlie Rose, Inc. under state law by an intern for PBS's *The Charlie Rose Show* (53 DLR A-14, 3/19/12).[1]

Depending on the outcome of these very recent cases, filings based on misclassification of interns could continue to increase. If successful, the misclassified interns would be entitled to back pay, liquidated damages, attorneys' fees, and costs under the FLSA. This can add up to a significant financial liability for employers, especially those who regularly use a large number of interns, not to mention a shift in the way certain industries conduct business. As a result, these cases will be watched closely by employers and the plaintiffs' bar alike.

[1] Although this article has focused on classification of unpaid interns under the FLSA, employers must also comply with any applicable state law requirements. Whereas many states apply similar tests as those under the FLSA, the tests under some states' wage-and-hour laws differ. New York's applicable wage-and-hour law, under which the Charlie Rose lawsuit was filed, uses a test similar to WHD's test but includes some additional but similar criteria, such as that the intern not receive employee benefits.

Tips to Avoid Unpaid Intern Litigation and Liability

Given the varying tests that have been applied in determining whether an unpaid intern should be classified as an employee under the FLSA, compliance with the FLSA with respect to unpaid interns may seem like a daunting task, especially for employers operating in multiple jurisdictions. Employers would be wise to structure their internship programs to comply with WHD's test, which is the most restrictive of the tests applied under the FLSA.

The following are examples of precautions employers can take in structuring their internship programs so as to comply with the FLSA:

■ Employers that are genuinely providing an educational experience for an intern are more likely to be in compliance with the FLSA so long as the internship is not merely a trial period for potential employees. Toward that end, employers should consider structuring their internship programs in collaboration with local universities or vocational schools so that students receive academic credit for participation in the program.

■ Interns should not perform janitorial, clerical, or other work that employees would normally perform. Creating faux assignments that may be of some benefit to the employer later is a great way to engage interns without the work being ''productive'' for the employer. Alternatively, interns could be given reports or substantive work already completed by an employee but which would be educationally beneficial to the intern.

■ The employer should consider developing training programs or events for its interns. By way of example, the employer may have its interns shadow different employees for a portion of the internship or observe special events or happenings important to the employer's operations.

■ The training that an intern receives during the internship should be targeted at an industry or occupation, rather than the employer's operations only.

■ Interns should be more closely supervised than the employer's regular employees.

■ Interns should not be referred to as ''employees,'' ''hires,'' or similar terms that would suggest an employment relationship.

■ If the intern is to be provided with a stipend to cover certain costs or events, the stipend should not be referred to as wages or compensation for work performed.

■ Prior to accepting the internship, the intern should be required to sign a document expressly stating that the intern is an intern and not an employee, that the internship is unpaid, and that the intern is not entitled to a job at the conclusion of the internship. The employer may also want to include other acknowledgements, such as that the internship is being provided in connection with a specific academic program or to provide training similar to that offered in a specific vocational program.

These are some significant steps employers can take to reduce the risk of potentially costly private litigation or government audits. Employers, however, would be

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wise to revisit any established internship programs for compliance with these standards and adhere to them when constructing new internship opportunities.