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Second Circuit Adopts "Primary Beneficiary" Test to Determine Whether Interns Fall Outside the Statutory Definition of "Employee"

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On July 2, 2015, the U.S. Court of Appeals for the Second Circuit reversed a federal district court decision that had held that certain unpaid interns should have been classified and paid as employees under both the federal Fair Labor Standards Act ("FLSA") and the New York State Labor Law ("NYLL"). *Glatt v. Fox Searchlight Pictures, Inc.*, Nos. 13-4478-cv, 13-4481-cv (2d Cir. July 2, 2015).[1]

In so holding, the Second Circuit acknowledged that the U.S. Supreme Court has yet to address the difference between unpaid interns and paid employees under the FLSA, although the Second Circuit noted that, in 1947, the Supreme Court held in *Walling v. Portland Terminal Co.*, 330 U.S. 148 (1947), that brakemen trainees were not employees. In reaching its decision in *Portland Terminal*, the Supreme Court relied on the following factors: the brakemen trainees did not displace regular employees and their work did not expedite the company's business, the trainees did not expect to receive any compensation and would not necessarily be hired upon successful completion of the training, the training course was similar to one offered by a vocational school, and the company received no immediate advantage from the trainees' work.

In response to *Portland Terminal* and subsequent developments, in 1967, the U.S. Department of Labor ("DOL") issued "informal guidance" on trainees as part of its Field Operations Handbook. Further, in 2010, the DOL published similar guidance, specifically pertaining to unpaid interns at for-profit enterprises, in an Intern Fact Sheet. Both publications list the same six factors for determining whether trainees/interns (as applicable) are employees. Specifically, the Intern Fact Sheet states

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[1] In the *Fox Searchlight* case, the Second Circuit also reversed the district court's decision granting class certification for a proposed class of intern plaintiffs. In denying class certification, the Second Circuit noted that

> the question of an intern's employment status is a highly individualized inquiry. [And the plaintiff's] common evidence will not help to answer whether a given internship was tied to an education program, whether and what type of training the intern received, whether the intern continued to work beyond the primary period of learning, or the many other questions that are relevant to each class member's case.

that interns fall outside the definition of "employee" and, therefore, need not receive minimum wage and overtime pay, *only if all six* of the following factors apply:

1. the internship 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 and works under the close supervision of existing staff;

4. the company derives no immediate advantage from the intern's activities (and on occasion, its operations might actually be impeded);

5. the intern is not entitled to a job with the company at the conclusion of the internship; and

6. the company and the intern understand that the internship is unpaid.

In its *Fox Searchlight* decision, the Second Circuit expressly declined to defer to the DOL's six-part test, stating that, unlike court deferral to an agency's interpretation of a statute or regulation, the DOL here was interpreting the Supreme Court's decision in *Portland Terminal* and improperly trying to fit the particular facts in that case to all workplaces, and the test was therefore "too rigid." Indeed, the Second Circuit noted that nothing in the Supreme Court's *Portland Terminal* decision suggests that any particular fact was essential to the conclusion reached, or that the facts on which the Supreme Court relied would have the same relevance in every workplace.

Instead, the Second Circuit held that the DOL and the courts should weigh all the factors addressed in *Portland Terminal*, considering the totality of the circumstances, and focus on whether the company or the intern was the "primary beneficiary" of the relationship. (According to this test, an intern would not be an employee if he or she is the primary beneficiary of the internship.) In this regard, the Second Circuit suggested that the following factors be considered:

1. The extent to which the intern and the employer clearly understand that there is no expectation of compensation. Any promise of compensation, express or implied, suggests that the intern is an employee—and vice versa.
2. The extent to which the internship provides training that would be similar to that which would be given in an educational environment, including the clinical and other hands-on training provided by educational institutions.
3. The extent to which the internship is tied to the intern's formal education program by integrated coursework or the receipt of academic credit.
4. The extent to which the internship accommodates the intern's academic commitments by corresponding to the academic calendar.

5. The extent to which the internship's duration is limited to the period in which the internship provides the intern with beneficial learning.
6. The extent to which the intern's work complements, rather than displaces, the work of paid employees while providing significant educational benefits to the intern.
7. The extent to which the intern and the employer understand that the internship is conducted without entitlement to a paid job at the conclusion of the internship.

The Second Circuit stated that in applying these factors, no one factor is determinative and every factor need not point in the same direction. Further, these factors are non-exhaustive, and courts may consider other relevant evidence beyond the specified factors in appropriate cases.[2]

What Employers Should Do Now

Employers located in states that are under the jurisdiction of the Second Circuit (New York, Connecticut, and Vermont) can breathe a little bit easier when it comes to using unpaid interns. At least for the time being, until the U.S. Supreme Court hears this or a similar case, interns need not meet the DOL's rigid six-factor test in order to be excluded from the definition of "employees" under the FLSA or NYLL.

Accordingly, in planning and implementing internship programs, employers in New York, Connecticut, and Vermont should:

- review their unpaid internship program(s) to ensure that, when analyzing the above seven factors, the intern is the "primary beneficiary" of the internship;

- work with those supervisors and others who may currently be managing internship programs to ensure that a majority of the factors listed above are met;

- review and revise, where applicable, summaries or other descriptions of existing or new internship programs to ensure compliance with the Second Circuit's guidance;

- in particular, ensure, to the extent possible, that interns receive academic credit for internships and/or that the internship corresponds with the academic calendar, and that the internship contains aspects similar to that which the intern would receive in an academic setting; and

[2] On July 2, 2015, the Second Circuit also decided another unpaid intern case, *Wang v. Hearst Corp.,* No. 13-4480-cv, which was argued in tandem with *Fox Searchlight*. In *Wang*, the U.S. District Court for the Southern District of New York had denied plaintiffs' motions (i) for class certification, finding that a determination as to the status of each intern required a highly individualized inquiry, and (ii) for summary judgment, finding that the facts were not all that clear, even after application of the DOL's six-part test. The Second Circuit affirmed as to the denial of class certification but vacated and remanded as to the denial of summary judgment, stating that the district court on remand should apply the standard that the Second Circuit announced in *Fox Searchlight*—i.e., whether the intern or the company was the "primary beneficiary" of the relationship.

- limit the length of internships to the period in which the internship provides the intern with beneficial learning—if an internship does not have a clear end date, this will likely be considered as a negative factor for a company seeking to maintain a lawful unpaid internship program.

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