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EXPERT ANALYSIS

2nd Circuit Adopts New 'Primary Beneficiary' Test for Determining If Unpaid Interns are Employees

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A recent wave of multimillion-dollar lawsuits brought against employers by unpaid interns demanding compensation for their work has resulted in settlements but no definitive word from the federal courts on when interns should be considered employees. Despite the volume of litigation in this area, the factors that federal district courts have considered to determine whether an intern must be paid have varied, leaving the issue unsettled — until July, when the 2nd U.S. Court of Appeals ruled on the issue.

On July 2, the 2nd Circuit in *Glatt v. Fox Searchlight Pictures,* 791 F.3d 376, held that a new test — the "primary beneficiary" test — should be used to determine whether an intern must be considered an employee and thus paid.

In 2014, NBCUniversal settled a class action brought by about 9,000 unpaid interns for $6.4 million. Other companies such as Viacom, Condé Nast, Warner Music Group and Lionsgate have similarly settled class-action lawsuits for amounts ranging from $1 million to $7.2 million.[1]

In reaction to the increasing number of lawsuits and multimillion-dollar settlements, companies have been terminating their unpaid internship programs or paying interns at least minimum wage.[2] Students have been left with fewer and more competitive internship options.

In *Glatt* three unpaid interns filed complaints against Fox Searchlight Pictures and Fox Entertainment Group, claiming they were entitled to compensation as employees under the Fair Labor Standards Act, 29 U.S.C. § 201, and the New York Labor Law.

Specifically, the plaintiffs alleged that the defendants had violated these laws by failing to pay them as employees during their internships, as required by minimum-wage and overtime provisions of the statutes. One plaintiff sought to certify a nationwide class.

DETERMINING EMPLOYMENT STATUS

In its decision, the 2nd Circuit rejected the U.S. Department of Labor's fact-sheet guidelines on unpaid interns working in the for-profit private sector. The DOL's fact sheet, issued in 2010, set forth a rigorous, intern-friendly test. The guidelines provided that there is no employment relationship only if all of the following six requirements are met:

- 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.
- The internship experience is for the benefit of the intern.
- The intern does not displace regular employees, but works under close supervision of existing staff.

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- 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.
- The intern is not necessarily entitled to a job at the conclusion of the internship.
- The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship.

In 2010 the New York State Department of Labor adopted the DOL's six-factor test and added five additional factors.[3] The NYDOL provides, just like the DOL in its guidelines, that an employment relationship does not exist only if all the criteria are met.

In *Glatt* the District Court used a version of the DOL's six-factor test. The lower court balanced the factors and found that four weighed in favor of finding that the interns were employees and the other two against, and ultimately it concluded that the interns were employees.

On appeal, neither party argued that the court should apply the DOL's guidelines.

The plaintiffs argued that when an employer receives an "immediate advantage" from an intern's work, the intern should be considered an employee. The defendants urged the court to adopt a "primary beneficiary" test in which the benefits to the intern are weighed against the value provided by the intern to the employer. The DOL filed an *amicus* brief urging the court to abide by the six-factor test.

The appellate court agreed with the defendants and adopted the primary-beneficiary test. The court wrote: "The primary beneficiary test has two salient features. First, it focuses on what the intern receives in exchange for his work. ... [S]econd, it also accords courts flexibility to examine the economic reality as it exists between the intern and the employer."

The 2nd Circuit articulated a list of non-exhaustive factors for courts to consider when determining whether the intern or the employer is the primary beneficiary of the relationship (see box).

The appeals court stated that no one factor is dispositive and that not every factor needs to point in the same direction to find that an intern is not an employee. The court emphasized that this decision reflects "a central feature of the modern internship — the relationship between the internship and the intern's formal education."

The 'primary beneficiary' test

The 2nd Circuit's "primary beneficiary" test includes these factors:

- 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.
- The extent to which the internship provides training that would be similar to that which would be given in an education environment, including the clinical and other hands-on training provided by educational institutions.
- The extent to which the internship is tied to the intern's formal education program by integrated coursework or the receipt of academic credit.
- The extent to which the internship accommodates the intern's academic commitments by corresponding to the academic calendar.
- The extent to which the duration of the internship is limited to the period in which the internship provides the intern with beneficial learning.
- 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.
- 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.

This approach allows courts to look to the totality of the circumstances, weighing and balancing all of the considerations at play in each unique case.

CLASS-ACTION CERTIFICATION

In addition, the court held that determinations under the primary-beneficiary test are "highly individualized inquir[ies]," meaning common, generalized proof required for certification of class actions would probably not be capable of answering the questions the court articulates in the test. Therefore, the court vacated the district court's orders certifying the plaintiffs' proposed class and the conditional certification of a nationwide collective action.

CONCLUSION

The primary-beneficiary test adopted by the 2nd Circuit emphasizes the educational aspects of internships and provides greater clarity to employers as to when unpaid internship programs are permitted.

The appeals court's decision is welcome relief for employers within the 2nd Circuit, including New York and Connecticut employers, that have traditionally offered opportunities to students via internship programs.

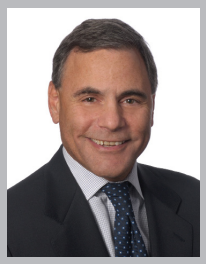
The court's rejection of any class or collective action in this case is a win for employers. Although the new standard does not explicitly preclude class actions by interns, the individualized nature of the test makes it unlikely that an employer will face lawsuits by large groups of current and former unpaid interns, such as those that led to the *Glatt* decision and the Viacom, NBCUniversal and other recent multimillion-dollar settlements.

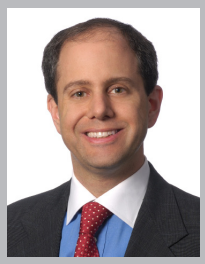
NOTES

[1] Many of the major lawsuits concerning unpaid interns have been in the media industry, probably because large numbers of unpaid internships tend to be much more prevalent in "high-prestige creative fields like music, media, and fashion." Neil Howe, *The Unhappy Rise of The Millennial Intern,* FORBES, Apr. 22, 2014. Unpaid interns, however, are used across all industries. Employers are bound by federal and state labor laws and the case law construing these laws.

[2] *See* Rachel Feintzeig & Melissa Korn, *Colleges, Employers Rethink Internship Policies,* WALL ST. J., Apr. 22, 2014; Melissa Schorr, *The Revolt of the Unpaid Intern,* BOSTON GLOBE, Jan. 12, 2014.

[3] NYDOL Opinion RO-09-0189 (Dec. 21, 2010).



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In a "primary beneficiary test," the benefits to the intern are weighed against the value provided by the intern to the employer.