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Whose Employee is it? Borrowed Servant, Agency, and Vicarious Liability Dangers

I. General Principles of Vicarious Liability.

Retail entities face liability not only for independent acts of negligence, but also for the acts of their employees via vicarious liability, or the more technical "respondeat superior." The principle holds that when an employee commits a tortious act while in the course and scope of her employment, her employer is likewise liable to the injured party for the transgression.

Many states, under workers' compensation statutes, provide employers with immunity from common law actions by their employees, for injuries they sustain on the premises or in the course of their duties.

In the context of discrimination and wage and hour laws, it is imperative to find out who exactly is the employer, and who is the employee, to determine if liability may attach.

But who, exactly, is an employee?

II. Borrowed Servant Principles.

Borrowed or loaned servant arrangements are common in the retail industry, and many others. Under such an agreement, one company agrees to borrow one or more servants who are actually employed with a different company, but are loaned to the company for a period of time or are dedicated to completing a very specific project.

The parties may have an agreement that the general employer will pay all of the employee's wages, provide workers' compensation coverage, and other benefits, and the "borrowing employer" will simply pay the employer for the right to borrow the employee.

Under this arrangement, both the General (original) employer and the special (Borrowing) employer may be considered to actually employ the individual -- in other words, there is legally a joint employment relationship.

You may owe the employee rights under the Family Medical Leave Act ("FMLA") (to provide leave and reinstate), or under other federal employment statues. It is a good idea to check the

workers' compensation and OSHA regulations of your state to see what your obligations are with respect to borrowed or loaned servants. Particularly, you need to make sure that you are covered by the exclusive remedy of the workers' comp. coverage so that the loaned servant cannot sue you (the special or borrowing employer) and or your employees in tort if there is an injury on your premises.

Sometimes the special employer may choose to voluntarily cover the loaned or borrowed or seconded employee under their comp coverage so that the exclusive remedy applies. Some states extend the exclusive remedy from the general employer to the special employer, so you just need to check your state's laws.

It is important to examine the facts closely when an issue of control by a defendant over a plaintiff arises. Most people falsely believe that the payment of wages is what determines the employer-employee relationship. It is not. Control is the important indica and control is often an element of establishing a relationship between the plaintiff and the defendant. If there is sufficient control by a defendant over a plaintiff to argue that the plaintiff is, in reality, an employee, the workers' compensation act immunity defense should be raised.

If the general employer retains control over the borrowed servant's actions, while he or she is working for the secondary employer, the general employer is usually vicariously liable for the tort. Alternatively, where the secondary employer directs the details of the borrowed servant's work, the secondary employer will likely be liable for the borrowed servant's torts under respondeat superior, and the general employer then is not liable. See Restatement Second, Agency § 227 (1958); id., comment a.

There is a distinction between the borrowed servant approach and an independent contractor. An independent contractor arrangement is distinct from the secondment agreement because the employer does not control the manner or means of the performance of services for the independent contractor. The independent contractor must supply their own tools and equipment and must essentially operate as a separate business selling services to more than one individual. In many states, the trend is to require that the IC does not work predominantly out of your offices. It is ok for the person to come into your office to perform specific duties, but their primary work space should not be in your office.

The body of law governing the classification of independent contractors as compared with servants is detailed and very state-specific. Some types of evidence that courts have considered to demonstrate an employer's control over a servant are: (1) the employer's right to discharge the employee; (2) the employer's payment of regular wages and workers' compensation insurance; and (3) long-term or permanent employment. Independent contractors, in contrast to servants, are more likely to have special skills, to be in business for themselves, to supply their own tools for the job to be performed, and to hire and fire their own employees. The Restatement (Second) of Agency § 220(2) provides additional guidance regarding the servant versus independent contractor distinction.

III. Pros and Cons of Independent Contractor Relationship Versus Seconded Employee

As far as the pros and cons, it really depends on the length of the project and what the person is going to be doing for you. If you expect to direct and control the person, and you expect them to work for a period of time out of your office, and you are borrowing the employee from another company, then you would use a secondment agreement. There really is no choice because that individual will not legally be an independent contractor. The con of this is that you are considered an employer and do owe some rights as an employer and can be sued on that basis.

With an Independent Contractor, the pro is that the person is not your employee, you do not owe any legal obligations to the person (ie, ADA, FMLA, Title VII). You do not have to provide workers' comp coverage, and have no specific reinstatement rights under any statute.

IV. Increasing Threat to Franchisors of Joint Employer and Agency Arguments for Employment Practices Liability and Related Claims.

A. The Rise of Claims in the Franchisor/Franchisee Context.

In recent decades, franchising has developed as one of the fastest growing and popular business models. A 2016 PwC study concluded that 801,000 franchises existed in the United States with 9 million in associated jobs, all of which contributed $541 billion toward the national gross domestic product. (PwC, "The Economic Impact of Franchise Businesses," Vol. IV, 2016).

The very success of the franchising model is directly attributable to its focus on creating a standard public image and the insistence on uniformity and consistency by franchisees. It is this control—inherent (and essential) to the franchise relationship—that plaintiffs' lawyers throughout the country have leveraged, with some success, to make direct employment practice liability ("EPL") claims against franchisors for personnel decisions made by franchisees.

EPL claims against franchisors have been slowly growing in frequency in recent years, and the expansion of "joint employer" theory is at the heart of this expansion. The law is in flux, with uncertainty about where it is headed. Franchisors are left to, in effect, "thread the needle" by creating a comprehensive franchise system designed to protect their intellectual property and proprietary systems, while carefully defining franchisee responsibility for personnel and human resource decision-making.

The theories being used by the plaintiffs' bar to hook in franchisors to liability for the wrongful actions of franchisee employees have taken many forms. The analysis applied to those claims differs on the statutes being used to sue (ie., wage and hour suits, versus negligence suits, versus discrimination statutes).

B. Common Factors Used to Analyze Franchisor Liability.

Some of the factors looked at by the courts when determining whether to impose liability on a franchisor for the acts of franchisee employees are:

1. actual authority to hire and fire the individual;

2. day-to-day supervision of the individual, including employee discipline;

3. whether the putative employer furnishes the equipment used and the place of work;

4. possession of and responsibility over the individual's employment records, including payroll, insurance, and taxes;

5. the length of time during which the individual has worked for the putative employer;

6. whether the putative employer provides the individual with formal or informal training;

7. whether the individual's duties are akin to a regular employee's duties;

8. whether the individual is assigned solely to the putative employer; and

9. whether the individual and putative employer intended to enter into an employment relationship.

The reaction of state legislatures to the wave of litigation has been swift with at least nineteen states having adopted one or more statutory provisions designed to protect franchisors. The result is a patchwork of state statutes which run the gamut from expressly prohibiting franchisors from being considered the employer of a franchisee's employees (*see*, *e.g.*, Ga. Code Ann. § 34-1-9 (2017)), to new statutes that allow for liability only upon a finding that a franchisor has "exercised a type or degree of control over the franchisee or the franchisee's employees not customarily exercised by a franchisor for the purpose of protecting the franchisor's trademarks and brand." (*See* Tex. Labor Code § 21.0022 (2015); *see also* Utah Code § 34-20-14 (2016)).

In reviewing the reported and unreported decisions where plaintiffs have made direct EPL claims against franchisors, a few common threads can be seen to run through these cases. Those include: a lack of clarity in the documentation of the franchise relationship; a failure to update documentation to reflect the actual way the businesses are operated; and a relationship between franchisor and franchisee in which the franchisor reserved for itself significant control over the day-to-day employment decisions of the franchise (whether such control was exercised or not).

C. Best Practices for Franchisors to Eliminate Risk from "Accidental Employees"

Broadly stated, the "best practices" to be considered by franchisors to avoid EPL claims can be summarized as follows:

Documentation/Discipline

- Franchisors must be aware of the risk of having franchisees utilize forms for hiring, employee discipline, complaint procedures, or other personnel issues which make reference to the franchisor in a way that can be exploited by plaintiffs' counsel;

- Franchisors should avoid any process whereby they are receiving grievances or complaints from the franchisee's employees about workplace conditions. Where complaints are received by the franchisor, they should be immediately forwarded to the franchisee for handling. Franchisees should be instructed to explain to their workers that they have one boss, and one employer;

- Franchisees should be directed to prominently include the name of the franchisee entity in all employee manuals, employment applications, vendor applications, business stationery, business checks, and the like. Franchisors should avoid providing "templates" to franchisees, who should be directed to retain competent advice from human resource professionals of their own choosing; and

- Franchisors should consider requiring franchisees to obtain signed acknowledgements from employees stating that the employee has been hired by the franchisee and no one else, that the franchisor is not his/her employer, and that the franchisor has no control over employment decisions.

Mandatory Systems and Policies

- While it is commonplace for franchisors to require that franchisees use a uniform point-of-sale system for reporting sales data, many of these programs have software features that include workforce management. If such features cannot be unbundled then it is important to make clear that you are not mandating use of the workforce management features; and

- Franchisors should not set specific work schedules for franchisees' workers, as the franchisees should control all aspects of the working schedule or assignment of particular workers to specific jobs. While it is ok to inform franchisees what jobs are needed to be done, it is too risky to tell a franchisee who must do the jobs. Nor should franchisors set minimum hours of work or limit dates of closure.

Reservation of control

- A reservation of authority by the franchisor within franchise agreements or other documentation that would, even theoretically, allow a franchisor to approve or disapprove of employees of the franchisee, or to terminate the franchise if certain personnel directives are not followed, can be used to show direct control sufficient for joint employer liability purposes; and

- Franchisors should review their agreements to see if there are holdover provisions from a safer era that are unnecessary to the operations and have become superfluous, yet could be used as a hook to argue that the franchisor has control over personnel decisions.

Inspections/Training

- Franchisor employees who conduct periodic inspections and who become engaged in day-to-day operations and disciplinary issues, or who take an active role in redirecting franchisee's employees or training them in any regard, create liability for the franchisor;

- Employees who visit franchise locations must be trained to avoid any involvement in employment matters, and franchisors should avoid any training of franchisees' employees other than management-level employees. When interacting with franchisee's employees, franchisor's employees should be trained to avoid any language or tone that could be viewed as authoritative or "top down"; and

- Reviews and inspections of franchisee operations are acceptable and justified by protection of a brand. However, where there is a violation of brand standards, there should not be any direction of the franchisee's employees. Rather, the franchisor should notify the franchisee of the inspection results and have the franchisee implement any corrective action. When communicating on this subject with the franchisee, the franchisor should be sure to explain that inspections are not done in lieu of their own duty to supervise *their own workers*.

Use of Brand Name

- Allowing franchisees to use the brand name when establishing their franchisee entities, or permitting franchisees to operate without prominently displaying placards on the premises giving notice that the business is an independently owned and operated business, creates significant risk. Establish a policy of disallowing the use of the brand name in franchisee operating companies, and require them to prominently state that they are separate and independently owned.