Joint Employment Can Have Expensive Consequences for Unsuspecting Cannabis Businesses Under California law and the Fair Labor Standards Act

By Meital Manzuri

The Fair Labor Standards Act's (FLSA) definition of "employer" contemplates the possibility of simultaneous employers, any one or all of which may be liable as an employer. The legal doctrine of joint employment, which states that an employee, or a group of employees, can be considered the employee of more than one employer at the same time, has strong precedent and ramifications under both the FLSA and California employment law. Under current practices, cannabis businesses increasingly engage cannabis employees by contracting with staffing firms, management companies, or other third-party arrangements for many reasons, including tax benefits, liability mitigation, operational ease, and loopholes in licensing restrictions. However, cannabis businesses should familiarize themselves with these laws to manage their liabilities as they may find themselves unwittingly in an employment lawsuit and subject to steep penalties.

The question then becomes, what cannabis business practices would extend liability under the doctrine of joint employment? In order to answer this question, one must first understand that, for federal FLSA purposes, there are two types of joint employment, horizontal joint employment and vertical joint employment. Where horizontal joint employment examines the relationship *between the potential employers;* vertical joint employment focuses on the *economic realities of the relationship between the employee and the potential joint employer*. Moreover, under California law an economic realities type of test would likely be applied. Read below for a full explanation of the legal analysis and how to examine workforce operations for potential liabilities.

Horizontal Joint Employment

Horizontal joint employment exists when two or more companies separately employ a worker and are sufficiently related to or affiliated with each other with respect to the employee. In horizontal joint employment situations, the employee will usually have an admitted employment relationship with each entity but may perform separate work and work separate hours for each.

Horizontal joint employment will generally be found in situations, such as: (a) arrangements between the employers to share or interchange the employee's services; (b) where the employers are associated "with respect to the employment of a particular employee and may be deemed to share control of the employee, directly or indirectly, by reason of the fact that one employer controls, is controlled by, or is

under common control with the other employer"[1]; or (c) where one employer acts directly or indirectly in the interest of another employer in relation to the employee - think management company that provides staffing as one of its services.

According to the Department of Labor, in determining whether two or more entities share sufficient control over the employee and thus would be categorized as horizontally joined, the following factors should be considered:

(1) Inter-mingled operations (e.g., same person scheduling and paying the employees, or one administrative operation for both employers);
(2) Shared clients or customers;
(3) Any overlapping managers, directors, officers, or executives;
(4) Shared control over operations (e.g., overhead costs, hiring, firing, advertising, payroll);
(5) Shared supervisory authority over the employee(s);
(6) Any agreements between the potential joint employers;
(7) One potential joint employer supervising the work of the other; and
(8) Treating the employees as a pool of employees available to both of employers.

Under the above test, a cannabis business that's found to have horizontal joint employment could be found liable for any number of torts and violations of employment law even though another entity caused this on the employee.

Economic Realities Test Used in Vertical Joint Employment under FLSA (and probably in CA Employment Law)

Conversely, in vertical joint employment there is an admitted relationship between the employee and one employer (the "intermediary employer") and the potential joint employer has typically contracted with the intermediary employer to provide it with labor and/or to perform certain employer functions, such as hiring or payroll, and the employee works for the benefit of the potential joint employer. As joint employers, each is responsible for the conduct of the other and whatever unlawful practices are engaged in by one are deemed to have been committed by both.

In evaluating whether a vertical joint employment relationship exists for purposes of the FLSA, the "economic realities test" requires courts to consider the totality of the circumstances of the potential employment relationship, including such factors as whether the alleged joint employer (1) had the authority to hire and fire the employee, (2) supervised and controlled the employee's work schedules and the conditions of his or her employment, (3) determined the rate and method of payment, and (4) maintained employment records.[2]

For example, in *Futrell v. PayDay*, the plaintiff worked on the set of Reactor Films and PayDay, a separate entity, processed Reactor Films' payroll. Plaintiff argued that PayDay was his joint employer

---

[1] See 29 CFR 791.2(b)

[2] *See* 29 C.F.R. § 791.2(a)(1)(1981); *Real v. Driscoll Strawberry Assocs.*, 603 F.2d 748, 754 (9th Cir.1979); *Bonnette v. California Health and Welfare Agency*, 704 F.2d 1465, 1470 (9th Cir.1983); *Futrell v. PayDay* (2d Cal.2010) 190 Cal. App. 4th 1419, 1430.

because, inter alia, it did the payroll for his primary employer and issued his paychecks. However, the court disagreed and found no employment relationship existed with PayDay. Specifically, the court noted that there was no evidence that PayDay exercised control over Futrell's hours or working conditions, plaintiff was not hired by PayDay, Reactor Films was the primary employer--not PayDay--and arranged and supervised the commercial shoots, and PayDay lacked control over plaintiff's hours and working conditions.[3] In light of the foregoing, the court went on to explain the lynchpin was whether PayDay "exercised control over workers' wages" by going beyond handling the ministerial tasks of calculating pay and tax withholding because it also issued paychecks, drawn on PayDay's own account. The court ultimately found this alone was insufficient to confer upon PayDay a joint employer relationship.

Accordingly, depending on the control that a cannabis business is exercising over the alleged joint employee, they can be found liable even if the other employer is the source of the legal violation.

Consequences of Joint Employment Under the FLSA

If any of the foregoing horizontal or vertical joint employer factors describe a company and other companies with which it has a relationship, then they probably share some employees. If so, the companies will all be responsible for ensuring that those employees that are not classified as exempt are paid at least minimum wage for the first 40 hours they work in each week and overtime pay for all hours worked in excess of the regular 40 hours in a given workweek. Each one of the employers will also be responsible for complying with any and all other requirements of the FLSA. The employee and the Department of Labor ("DOL") can pursue minimum wage and overtime claims and any other claimed breach of the FLSA against any one of the companies at issue either separately or together.

Beware of "Independent Contractors" in California

Passed in 2019, AB 5 tightened the reins on the classification of independent contractors and could impact joint employment liability issues as well. For example, a cannabis business that uses a staffing agency that has misclassified workers under AB 5, could be held jointly liable for the misclassification. One way in which cannabis businesses can protect themselves is to draft and execute an enforceable and comprehensive Master Service Agreement between the two entities that shifts the appropriate risk back to the staffing agency.

How Does this Impact Cannabis Businesses?

Cannabis companies that have employees involved with another entity, whether technically separate or not, need to consider the possibility of joint employment. For example, we regularly see management companies assisting licensees in setting up their operations, including providing employees to staff the licensed business. Similarly, there are numerous cannabis-specific staffing agencies that will send an employee to a location to work on a long- or short-term basis. In these

[3] 190 Cal. App. 4th at 1431-32, 1435.

scenarios, the management and staffing companies are intermediaries. While horizontal joint employment is less likely in these situations, cannabis companies need to look at whether they might be considered vertical joint employers by considering whether they can directly fire the employee, who sets the employee's schedule and rate of pay, which entity issues the employee's paycheck, and whether or not it maintains employee records.[4] The greater number of elements present increases the likelihood that a cannabis company will be jointly liable.

Additionally, the cannabis regulations allow two separate licensees on the same premises to share a security company.[5] The state regulations explicitly state that each licensee will be separately responsible for compliance with the security requirements and it is likely that courts would likewise find a vertical joint employment relationship.

Licensees should review their nonstandard working relationships to determine whether they constitute joint employment. They can mitigate their risks of being found jointly and severally liable for FLSA wage and hour violations by being vigilant about vetting the companies that they work with for compliance. When entering into an agreement with another company, e.g., a staffing company, adding a clause requiring the staffing company to provide indemnity and defense against FLSA litigation can also save the licensee thousands on litigation fees should a lawsuit arise. Finally, if an employee or the DOL seeks back pay from a cannabis company, it can then pursue from the other entity or entities contribution, or what is presumably their portion of the liability.

Meital Manzuri is the managing partner of Manzuri Law

[4] Maintenance of personnel records is mandated under the California commercial cannabis regulations. *See* 16 CCR Div. 42, § 5037(a)(2); 3 CCR Div. 8, § 8400(d)(7); 17 CCR Div. 1, Ch. 13, § 40500(a)(7).
[5] *See* 16 CCR Div. 42, § 5044(l).