From the Experts: Unpaid Internships' Swan Song?

Is a New Lawsuit the Swan Song for Unpaid Internships?

A new lawsuit tests the boundaries of internship programs.
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Many companies have a longstanding practice of engaging college students or other industry initiates as unpaid interns. These internship programs can provide benefits both to the interns and to the companies that engage them. What could be wrong with that? According to the U.S. Department of Labor, these arrangements could violate the Fair Labor Standards Act (FLSA).

Under the FLSA, "employees" must be paid at least minimum wage for all regular hours worked, and nonexempt employees must be paid overtime for all hours worked in excess of 40 per week. Companies argue that unpaid interns are not employees and are not covered by the FLSA. But this argument is muddied by the FLSA's broad and vague definitions of employee ("any individual employed by an employer") and employ ("to suffer or permit to work"). If an intern meets these definitions, then he or she could be covered by the FLSA and therefore entitled to wages.

The Department of Labor's Strategic Plan for Fiscal Years 2011-2016 makes clear that the department intends to devote significant resources in the coming years to ensuring that vulnerable workers—such as young workers and others not likely to file a complaint—receive all appropriate wages and overtime pay. Add to that commitment a new, high-profile lawsuit brought against Fox Searchlight Pictures, and companies are faced with the potential that their use of unpaid interns will take center stage.

Black Swan Interns Turn the Spotlight Onto Wage-and-Hour Issues

Two men who worked as unpaid interns on the 2010 Oscar-nominated film Black Swan have sued the film's production company for allegedly violating the FLSA and the New York Labor Law. The lawsuit hinges on the theory that the plaintiffs were classified as interns, but actually were employees who should have been paid for their work.

Key to the lawsuit will be a "Fact Sheet" issued by the Labor Department that articulates six criteria that a for-profit company must meet in order to lawfully engage an unpaid intern. According to the department, a company must satisfy all six of the following factors to properly treat an individual as an unpaid intern under 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 e:
4. The employer that provides the training receives no immediate advantage from the activ
   on occasion its operations may actually be impeded;
5. The intern is not necessarily entitled to a job at the conclusion of the internship; and
6. The employer and the intern understand that the intern is not entitled to wages for the time spent in the internship.

The Department of Labor's Fact Sheet explains that "the more the internship provides the individual with skills that can be used in multiple employment settings, as opposed to skills particular to one employer's operation, the more likely the intern would be viewed as receiving training." By contrast, "If the interns are engaged in the operations of the employer or are performing productive work (for example, filing, performing other clerical work, or assisting customers), then the fact that they may be receiving some benefits in the form of a new skill or improved work habits will not exclude them from the FLSA's minimum wage and overtime requirements because the employer benefits from the intern's work."

The department also noted, "If the employer would have hired additional employees or required existing staff to work additional hours had the interns not performed the work, then the interns will be viewed as employees entitled to compensation under the FLSA."

Unfortunately for companies engaging interns, the Department of Labor's test is difficult to apply. For example, the fact that companies must not derive immediate advantage from an intern's activities, while at the same time ensuring that the experience benefit the intern and approximate training the intern would receive in an educational setting, presents companies with a catch-22: They can allow the intern to do meaningful work, and thereby potentially run afoul of the requirement that the company derive no benefit from the intern's activities; or they can allow the intern to do nothing of substance, thereby failing to satisfy the requirements that the intern benefit from the experience and receive training that mimics the training they would receive in an educational setting. Either way, the company loses.

The Black Swan interns' lawsuit is a prime example of this problem. The complaint, filed in the U.S. District Court for the Southern District of New York, alleges that interns performed both substantive and menial work. These allegations will bring the Department of Labor's test to the forefront. To date, courts have offered little guidance on these issues. Thus, the Black Swan suit could become a test case for this area of the law.

How to Determine Whether Your Internship Program is a Swan or an Ugly Duckling

In analyzing the Department of Labor's criteria, it is important for companies to recall that they constitute mere guidance, and are not binding on courts. Thus, although the department takes the position that all six factors must be satisfied in order to avoid an employer-employee relationship under the FLSA, some courts do not take such a strict stance on the issue.

Employers should note, though, that even those courts that deviate from the specifics of the Department of Labor's criteria still adhere to the overarching ideas behind them, making it unwise for an employer to assume that a court will reject the department's guidance altogether.

For example, some courts employ a "totality of the circumstances" test, under which the Department of Labor's criteria are considered to be relevant but not determinative. Other courts look to whether the individual or the company principally benefits from the work performed, while others have opted to adhere to the department's criteria.

Unfortunately, as noted above, there is a dearth of case law offering concrete guidance to employers on the issue of treatment of unpaid interns. Thus, companies are navigating uncertain territory when they set out to determine whether their unpaid internship program passes muster under the FLSA. Additionally, it is important for companies to remember that their state's laws might impose even stricter requirements than the FLSA.

To determine the extent to which an unpaid internship program satisfies the Department of Labor's criteria, a company must carefully analyze all of the activities its interns engage in, and must evaluate the extent to which the company relies upon those interns in its daily operations. The more indispensable a company's interns are to its operations, the more likely it becomes that those interns will be considered employees under the FLSA who must be paid for their hours worked.

Companies should conduct this analysis with the involvement of counsel to increase the possibility that their efforts will be protected from disclosure if an intern challenges the company's practices or if the Department of Labor comes calling.

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