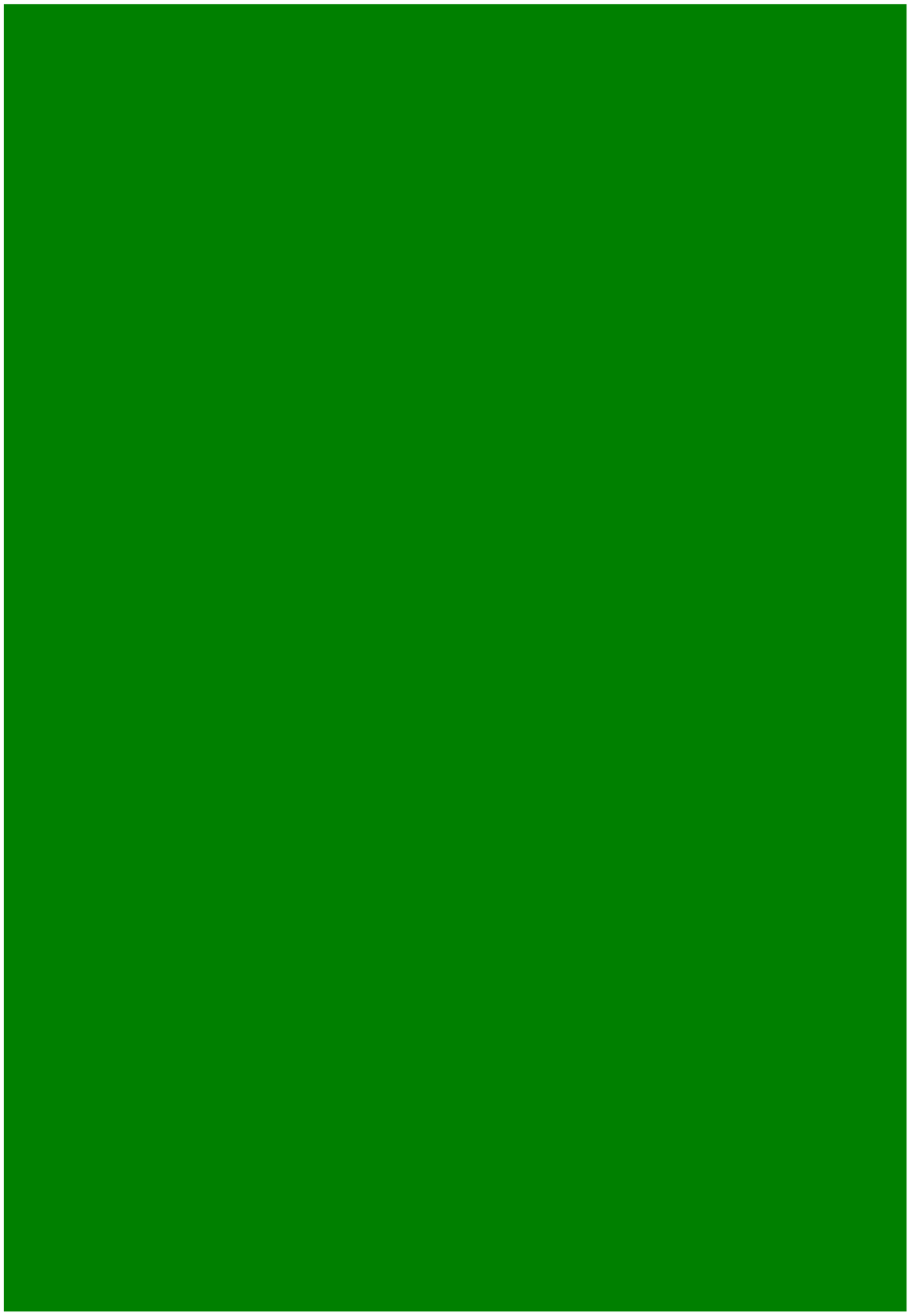
PERSONAL LIABILITY OF CORPORATE AGENTS:

CASTING ASIDE THE NOTION THAT THERE IS NO INDIVIDUAL LIABILITY UNDER THE FLSA

BY JILL GARCIA, ESQ.

As all employers know, the acts, omissions and misdeeds of their employees can often lead to lawsuits against their companies. Employers are also acutely aware that the company will be liable when a manager or director makes payroll or personnel decisions that violate state and federal wage and hour laws. The result is employers paying for the damages caused or created by their representatives. While most managers and directors are aware that they may be held personally liable for torts they commit while at work, many do not realize that they can be held personally liable for their policies, decisions and actions which result in violations of federal wage laws. This should be an eye-opener for many management employees.



While companies are going bankrupt at an alarming rate, the Ninth Circuit has just given plaintiffs a reason to head to federal court with wage and hour claims even after the company has sought shelter under bankruptcy proceedings or has closed its doors. On July 27, 2009, the Ninth Circuit announced in *Boucher v. Shaw* that individual managers can be held personally liable for wage and hour violations under the Fair Labor Standards Act (FLSA) even if the company that employed the plaintiffs has filed for bankruptcy.[1]

The *Boucher* opinion serves as a practical reminder of potential *personal liability* of corporate agents for their pay practice policy determinations – of particular concern when a company files for bankruptcy or is insolvent and has outstanding wage and overtime obligations.

Background

In *Boucher*, the plaintiffs' employer, the Castaways Hotel, Casino and Bowling Center, filed for Chapter 11 bankruptcy protection in June 2003. In January 2004, Castaways, operating as a debtor-in-possession, terminated the three plaintiffs. The following month, the Castaways Chapter 11 petition was converted to a Chapter 7 liquidation, and Castaways ceased all operations.

Later that year, the discharged plaintiffs filed a class-action suit in Nevada District Court against three senior Castaways managers (the CEO, the manager of employment issues and the CFO) for unpaid wages under state and federal law. Castaways was not named as a defendant. Essentially, plaintiffs alleged that each individual corporate executive was an "employer" under the applicable state and federal statutes.

The Ninth Circuit Certifies the Issue of Individual Liability to the Nevada Supreme Court

Following removal of the action to federal court, the managers moved to dismiss the claims based, in part, upon the fact that Castaways had filed for bankruptcy protection. The managers maintained that they should be afforded the same bankruptcy protections as the corporate employer. The District Court dismissed the Nevada state wage and hour claims and the FLSA claims. The plaintiffs appealed.

On appeal, the Ninth Circuit asked the Nevada Supreme Court to address whether the managers could be deemed "employers" under NRS 608.011. Because of the "significant implications for Nevada's wage protection law," the issue was certified to the Nevada Supreme Court.

The Nevada Supreme Court Rejects Individual Liability

The Nevada Supreme Court returned with an opinion that individual managers could *not* be

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held liable as "employers" under Chapter 608. The court was unwilling to expand the statutory definition of "employer" to include individual employers absent a clear expression of legislative intent.[2] Being that NRS 608.011 defines an employer as "every person having control or custody of any employment, place of employment or any employee,"[3] the Supreme Court was unwilling to classify individual managers or supervisors as employers. Accordingly, the plaintiffs' state law claims were dismissed.

However, the question of whether individual managers were considered employers under the FLSA had yet to be resolved.

Background Regarding the FLSA

The FLSA governs minimum wage, overtime, recordkeeping, exemptions, equal pay, child labor and timely payment of wages. Penalties for violation of the FLSA include liability to the employee for their unpaid minimum wages or their unpaid overtime, as the case may be, and in addition, an equal amount as liquidated damages.[4]

Are Corporate Agents "Employers" Under the FLSA?

The FLSA defines an employer as "any person acting directly or indirectly in the interest of the employer in relation to an employee...."[5] Earlier Ninth Circuit decisions determined that the definition of "employer" was to be given an "expansive interpretation in order to effectuate the FLSA's broad remedial provisions."[6] The cornerstone of the inquiry was the "economic reality" of the employment relationship. Under this mandate of broad interpretation, if an individual exercises "control over the nature and structure of the employment relationship" and "economic control," he or she is an employer under the FLSA, and thus subject to personal liability.[7] Factors considered in determining the "economic reality" include operational control of significant aspects of day-to-day functions, the power to hire and fire employees, the power to determine salaries and responsibilities with respect to employment records.[8]

Other circuits have reached similar conclusions. For instance, the Second Circuit, in *Herman v. RSR Sec. Servs.*, found that a part owner of a corporation could be held personally liable for FLSA violations where he interfered in business affairs and had considerable control of employees.[9] While this owner was not directly involved in daily supervision of employees, his financial control, involvement in business affairs and direction with respect to employment issues were sufficient under the economic realities test.[10] Similarly, the Fifth Circuit, in *Donovan v. Sabine Irrigation Co.*, noted that the determination of an "employer" under the FLSA is not based upon "formalistic labels or common-law notions of the employment relationship," but instead upon the economic realities of the workers' employment.[11] In *Donovan*, a corporate officer with no ownership interest was deemed an "employer" based upon his monetary infusions, policy direction and that, ultimately, the corporation operated for his benefit. In *Dole v. Elliott Travel Tours, Inc.*, the Sixth Circuit deemed a corporate owner and president an employer where he controlled the proverbial "purse strings" of the corporation.[12]

Thus, a liable corporate agent – not defined by title but instead by the economic realities of his relationship with the employee – could potentially be an owner, an officer, a director or even a human resources manager. This determination is going to be made based upon, in essence, the question "Does this individual have economic control over the employees and does this person have the authority to make policy decisions?"

Are the Corporate Officers Liable for Violations of the FLSA?

Since the individual defendants did not challenge their status as "employers" under the FLSA, the remaining issue was whether Castaways' bankruptcy affected the individual defendants' liability for unpaid wages. The individual defendants "argue[d] that any duty they had to pay wages... ended with the conversion of the Castaways' Chapter 11 bankruptcy proceeding into a Chapter 7 liquidation."[13] Essentially, the defendants reasoned that since they stood in the stead of the corporate employer in this FLSA claim, and the corporate employer was protected from the claim by the bankruptcy, they too should be entitled to identical bankruptcy protection.

Not according to the Ninth Circuit. The court explained, "we cannot see how it makes a difference one way or the other whether the Castaways was in Chapter 11 or Chapter 7. The Castaways is not a defendant, and the defendants are not debtors."[14] After further analyzing the automatic stay afforded under bankruptcy law, the Ninth Circuit noted

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that the automatic stay does not extend to non-debtors or their property. While the court had not previously addressed whether a company's bankruptcy affects individual liability under the FLSA, it now held that "our case law regarding guarantors, sureties and other non-debtor parties leaves no doubt about the answer: the Castaways bankruptcy has no effect on the claims against the individual managers at issue here."[15]

In reaching this conclusion, the Ninth Circuit noted that it had found at least two cases wherein corporate agents were held liable under the FLSA following a corporate bankruptcy.[16] Ultimately, the Ninth Circuit affirmed the dismissal of the state law claims, but reversed the dismissal of the FLSA claim.[17]

Potential Pitfalls of the FLSA for Corporate Employers and Managers Alike

Potential minefields await the manager dabbling in the realm of federal wage and hour law. Common misconceptions include:

- If I put an employee on a salary, he becomes exempt.
- If an employee has a manager, supervisor or administrator title, he is exempt.
- If an employee is highly compensated, he is exempt.
- If an employee has an advanced degree, he is exempt.

While, in many circumstances, any number of these employees may be exempt from the FLSA's overtime provisions, a careful understanding and review of the statute, applicable regulations and surrounding case law is essential to proper application of the FLSA.

In Light of Boucher, How Can Individual Managers Minimize Their Risks?

Given the minefields awaiting detonation, how can an individual manager, director or owner limit potential exposure under the FLSA? While there is no easy answer to avoiding exposure to liability under the FLSA, managers should take the following steps:

- Engage in appropriate pay practices.
- Conduct an internal audit to ensure employees are properly paid under both federal and state law. The audit should include ensuring compliance with minimum wage and overtime obligations as well as appropriate employee classification.
- Utilize training opportunities. Ignorance of the law is not an excuse for non-compliance.
- Ensure managers are trained in wage and hour law and understand their own obligations regarding the same.
- Maintain appropriate time records.
- Involve the experts. When questions arise, be sure to consult human resources professionals and employment counsel before making uncertain wage and hour decisions.

The Implications of Boucher

Boucher has significant implications for the FLSA's wage protection law. FLSA lawsuits are the most common lawsuits filed in federal court. Cases like *Boucher* should serve to remind managers, officers and owners to ensure they are in compliance with appropriate pay practices as they may eventually be held personally liable for any violations.

In these difficult economic times, as the number of bankrupt and insolvent employers rises, lawsuits against individual owners and managers with the potential means to pay corporate debt will likely be on the rise as well. Thus, the implications of personal liability must be considered by employers and management employees alike, particularly with respect to corporate pay practices. NL

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1 *Boucher v. Shaw*, 572 F.3d 1087 (9th Cir. 2009).
2 *Boucher v. Shaw*, 196 P.2d 959, 960 (Nev. 2008).
3 NRS 608.011.
4 29 U.S.C. § 203(d).
5 29 U.S.C. § 203(d).
6 *Lambert v. Ackerley*, 180 F.3d 997, 1011-12 (9th Cir. 1999) (en banc).
7 *Id.* at 1012.
8 *Id.*
9 172 F.3d 132 (2nd Cir. 1999).
10 *Id.* at 141.
11 *Donovan v. Sabine Irrigation Co.*, 695 F.2d 190, 195 (5th Cir. 1983).
12 942 F.2d 962, 966 (6th Cir. 1991).
13 *Boucher*, 572 F.3d at 1091.
14 *Id.* at 1092.
15 *Id.* at 1093.
16 *Id.* at 1094 (citing *Donovan v. Agnew*, 712 F.2d 1509, 1511, 1514 (1st Cir. 1983); *Chung v. New Silver Palace*, 246 F. Supp. 2d 220, 226 (S.D.N.Y. 2002)).
17 *Boucher*, 572 F.3d at 1094.