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Redefining the Internship in the Face of Legal Realities and Economic Valuations

Abstract

[Excerpt] College internship programs have received considerable attention in the past four years since the U.S. Department of Labor (the “DoL”) issued a fact sheet aimed at educating employers and schools about the application of the Fair Labor Standards Act (the “FLSA”) to such programs. Highly publicized law suits followed. The prevailing view that seems to be emerging is that an intern, who works alongside paid employees and performs productive work for an employer, should be treated as an employee and paid at least the applicable minimum wage. While the debate is far from being settled, one thing is clear today: college credit is not an alternative to a paycheck, not only from an economic, but also from a legal perspective. Some employers have forced interns to register for college credit, whether the student needed the credit for graduation or not, believing that registration for credit exempted the intern from the reach of the FLSA. Such practice forced some students not only to work without wages but also to pay significant tuition costs for the privilege of working. Second circuit courts have ruled that whether college credit is granted or not should be between the student and the college and does not have much bearing on the employer’s compliance with employment laws.

Keywords

HR Review, Human Resources, Internships, FLSA, Minimum Wage, Training

Disciplines

Benefits and Compensation | Human Resources Management | Labor Relations | Training and Development

Comments

Suggested Citation

Lorenz, M., Thomas, W. L. (2015, April 14). Redefining the internship in the face of legal realities and economic valuations. *Cornell HR Review*. Retrieved [insert date] from Cornell University, ILR School site: <http://digitalcommons.ilr.cornell.edu/chrr/75>

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CORNELL HR REVIEW

REDEFINING THE INTERNSHIP IN THE FACE OF LEGAL REALITIES AND ECONOMIC VALUATIONS

Magdalena Lorenz and Wade L. Thomas

College internship programs have received considerable attention in the past four years since the U.S. Department of Labor (the “DoL”) issued a fact sheet aimed at educating employers and schools about the application of the Fair Labor Standards Act (the “FLSA”) to such programs.¹ Highly publicized law suits followed.² The prevailing view that seems to be emerging is that an intern, who works alongside paid employees and performs productive work for an employer, should be treated as an employee and paid at least the applicable minimum wage.³ While the debate is far from being settled, one thing is clear today: college credit is not an alternative to a paycheck, not only from an economic, but also from a legal perspective. Some employers have forced interns to register for college credit, whether the student needed the credit for graduation or not, believing that registration for credit exempted the intern from the reach of the FLSA.⁴ Such practice forced some students not only to work without wages but also to pay significant tuition costs for the privilege of working. Second circuit courts have ruled that whether college credit is granted or not should be between the student and the college and does not have much bearing on the employer’s compliance with employment laws.⁵

As a result, many employers have eliminated their unpaid internship programs altogether.⁶ Some employers have created paid internship programs, which serve as a recruiting tool, designed to attract new talent and screen candidates for future permanent employment.⁷ The current discussion around whether a college intern should be treated as an employee under the FLSA, has been an all-or-nothing proposition. In fact, if a for-profit employer is paying an intern a sub-minimum wage, such employer stands less chance of defending its legal position than an employer who pays an intern nothing.⁸ Is this really what Congress intended? Does it make sense from the economic standpoint?

The focus of this article is to help HR professionals understand the regulatory framework surrounding internships and make decisions about their existing internship programs. The authors also examine a statutory exemption which allows payment of subminimum wages to “learners”⁹ and propose improvements to current regulations to make the exemption applicable to internship programs. The article argues that perhaps the all-or-nothing approach currently applied to internship programs is not the best solution. As the national debate over increasing the federal minimum wage intensifies and the lawsuits involving unpaid college internships multiply,¹⁰ this is a timely discussion which merits attention and action of courts and legislators.

The Legal Framework

The FLSA mandates that all employers covered by the law pay at least minimum wage to their employees.¹¹ The statute itself contains no exemptions for interns. Instead, employers offering unpaid internships have relied on an exemption carved out by the Supreme Court in *Walling v. Portland Terminal Co.*¹² The case involved a week-long training program for brakemen conducted by a railroad shipyard.¹³ The High Court held that the brakemen-in-training were not employees within the meaning of FLSA.¹⁴ Rather, they were trainees, shadowing the regular employees for the learners' own benefit.¹⁵ And so a door was opened, which, decades later, resulted in entire companies relying on unpaid work of student interns.

In 2010, the DoL issued a set of guidelines concerning unpaid internships in a for-profit setting, Fact Sheet # 71: Internship Programs Under the Fair Labor Standards Act (the "Fact Sheet"). The Fact Sheet states six conditions, all of which have to be met in order for the internship to be unpaid.¹⁶ The most controversial of the factors states that when the employer derives any "immediate advantage" from the work of the intern, the intern should be paid. Many, including the authors, interpret it to mean that an unpaid intern cannot perform any productive work that benefits the employer.¹⁷

Two highly publicized lawsuits followed. Most notably, in *Glatt v. Fox Searchlight Pictures*, the District Court adopted the DoL guidelines as the applicable test whether an intern working in a for-profit setting should be classified as an employee.¹⁸ The court certified a class action with a representative plaintiff being an intern not registered for college credit.¹⁹ The court regarded college registration to be of minor significance in determining whether the intern should be classified as an employee.²⁰

The DoL Fact Sheet and the *Fox Searchlight* case spawned dozens of law suits. Research reveals over 30 cases involving interns in the past three years.²¹ The *Fox Searchlight* case is currently being appealed. Time will show what legal standard for measuring the lawfulness of unpaid internships emerges from the litigation. But is it really appropriate for the courts to craft a wholesale exemption to the FLSA? As justice Sotomayor wrote, evaluating the Pathways to Employment training program in one of the cases where the defendant claimed the "trainee" exemption:

[The] question of whether such program should be exempted from the minimum wage laws is a policy decision either Congress or the Executive Branch should make...[The] Court... cannot grant an exemption where one does not exist in law.²²

Interestingly, perhaps Congress has already done so, but the DoL made sure that few will use it.

Exemption for “Learners”

Section 14(a) of the FLSA authorizes the DoL to issue regulations allowing employers to pay “learners and apprentices” lower wages than the statutory minimum.²³ The statute envisions that the employers who wish to avail themselves of the exemption would apply for a certificate.²⁴ The DoL could then decide and monitor any employment at subminimum wages. FLSA does not specify how little a “learner” could be paid or for how long the exemption would be available with respect to any single employee/learner – that is left for the DoL. The DoL also defines who are “learners” or “apprentices.”

The plain reading of the provision indicates that Congress did indeed contemplate at the beginning that individuals who need training would be paid less than regular employees. So, why all the litigation and court-created trainee exemption? Are college interns not what Congress called in 1938 “learners” or “apprentices”? Not according to the DoL.

A quick perusal of the attendant regulations shows that the exemption would squarely not be applicable to college interns. Among other requirements, the regulations state that the certificates allowing sub-minimum employment would not be issued to anyone working in “office and clerical occupations in any industry.”²⁵ Most of today’s college interns work in an office setting. That prohibition alone eliminates most internship programs from consideration. Who are today’s “learners” then according to the DoL?

The regulations do not shed much light on the specific types of workers the DoL envisioned as qualifying as learners. It is hard to conceive examples of contemporary employment that fit the DoL’s arcane definitions, that is, jobs not performed in an office or clerical setting and also not qualifying as “skilled trade,” as required by regulations. Certain workers training for positions in manufacturing would likely fit the definition. The economy’s shift from manufacturing to services over the past 80 years perhaps warrants revisions to the regulations to better reflect the congressional intent behind establishing the exemption.

Complex regulations also govern the application process for a certificate authorizing payment of a subminimum wage. The applicant must show, among other requirements, that no employees were available for employment at least the minimum wage.²⁶ The local Department of Labor office has to provide written evidence to that effect.²⁷ Information that must be gathered and submitted with the application includes an explanation of “why employment at subminimum wage is needed to prevent curtailment of employment opportunities.”²⁸

What does the employer gain after the successful completion of the arduous process? If the training program is not affiliated with any school, the maximum saving to the employer is \$87 per employee.²⁹ If the training program is affiliated with a school, the savings rise from 5%³⁰ below the applicable minimum wage to 25% for the duration of the school year.³¹ Why would rational employers go through the complex and time-consuming procedure to effectuate such insignificant savings?

Evidence suggests they would not.³² Use of Section 14(a) with respect to learners has proven to be quite limited and skewed lopsidedly to 3 jurisdictions.³³ DOL data for the period 2009-2013 reveal just 1,609 applications processed for nine states and the Commonwealth of Puerto Rico.³⁴ Exceptions to the minimum wage provisions of the FLSA are dominated by Puerto Rico at 1,284.³⁵ Texas is in second place with 290, followed by Illinois with 21.³⁶ Finally, the number of applications processed overall is declining.

Significance of Section 14(a) Exemption to College Internship Programs

We argue that the regulations accompanying the exemption would currently not allow for most employers to sponsor an unpaid college intern. Additionally, as the data show, the cumbersome procedures provide employers little incentive to even go through the application process. Altogether, this renders the exemption not very relevant nor appealing to employers wishing to employ “learners.” The *status quo* cannot be what Congress had envisioned when they created the exemption.

The plain reading of the statute shows a clear framework for how the FLSA was to apply to individuals with little experience, in today’s terms: “interns.” As Justice Black explained in *Walling v. Portland Terminal*:

Many persons suffer from such physical handicaps, and many others have so little experience in particular vocations that they are unable to get and hold jobs at standard wages. Consequently, to impose a minimum wage as to them might deprive them of all opportunity to secure work, thereby defeating one of the Act's purposes, which was to increase opportunities for gainful employment. On the other hand, to have written a blanket exemption of all of them from the Act's provisions might have left open a way for wholesale evasions. Flexibility of wage rates for them was therefore provided under the safeguard of administrative permits.³⁷

In sum, individuals who are learning their jobs were to be covered by FLSA, but under Sec. 14(a), under the supervision of the Wage and Hour Administrator, the employers were to be allowed to pay them less than minimum wage. The current regulations certainly do not serve that purpose. Instead, the DoL served the public with the Fact Sheet, taking an all-or-nothing approach.

The Fact Sheet, issued by the DoL and intended to educate employers and eliminate many unpaid internships, stirred up litigation while unpaid internships in the for-profit sector have not gone away. According to a survey conducted by National Association of Colleges and Employers, about half of internships taken by students graduating in 2013 were unpaid.³⁸ Thirty-eight percent of unpaid internships were in the for-profit sector, where internships are subject to the FLSA.³⁹ That means that scores of employers regarded their interns as excluded from the definition of “employee” under the FLSA.

The result is a shadow economy of unpaid interns and exactly the wholesale evasions that Justice Black warned about in the absence of DoL supervision. By eliminating the use of

Sec. 14(a) with respect to learners, the DoL abdicated its role in supervising wages of such learners. Instead, the role was given to the courts to resolve disputes between interns and employers on a case-by-case basis. This is not a very efficient way of dealing with an issue that affects such a large segment of our economy.

Proposed Changes

The authors propose that the DoL revisit the regulations under Section 14(a) to make them relevant to internship programs and today's economy.⁴⁰ It is not in the power of the DoL to repeal a subminimum wage exemption, but that is what effectively has taken place with respect to "learners" under Section 14(a). The DoL should be overseeing internship programs, not fighting to eliminate them.⁴¹

In order to accomplish that, the authors suggest regulatory changes in three respects: (a) expanding the definition of learners/student learners to make the exemption applicable to college internships; (b) simplifying the application process; and (c) increasing the incentives for employers to apply for the certificates. The expanded definition of learners ought not prohibit issuing certificates in office and clerical occupations, as the current regulations do⁴² or requiring that the program be a "vocational training program."⁴³

The authors propose central handling of all applications by a single office of the DoL rather than sending employers to contact a regional office and requiring the collection of all sorts of esoteric information.⁴⁴ The DoL should consider requiring that applications for certification be signed by an accredited educational institution where the student intern is seeking a degree. A college internship coordinator is arguably in a better position than the DoL to set the learning goals and objectives, assess the student-learning outcomes, and monitor students' progress of a particular internship program. Rather than requiring the employer to complete a certificate for each student, certificates could be issued for an internship program affiliated with a particular educational institution – this would help streamline the process. Certificates could be issued for a term such as the duration of the school year.

Finally, the employers should be given incentives that are greater than the current 75 to 95% reduction in the minimum wage to apply for the certificates and employ student interns. Just to take one practical example, allowing a 50% reduction in pay would currently save the employer of a student intern earning 3 college credits \$435.⁴⁵ Nonetheless, the wage costs paid to the student intern represent only a portion of the total costs borne by the employer. Adding a student intern to the payroll is accompanied by FICA taxes or state unemployment and workers' compensation insurance. But the alternative of practice of excluding student interns from the definition of an "employee" does not seem to have a solid legal basis under the FLSA.

Summary: Advice for the HR Professional

If an internship program resembles the Portland Terminal brakemen training program, which gave rise to the "trainee exemption"--that is, students are shadowing employees for

a week on the employer's premises the employer is on safe grounds to not treat interns as paid employees. On the other hand, if a company subscribes to “learning by doing,” like almost all employers we know of who offer internship programs, it could be time for serious reconsideration of the features of the internship. If students come on the employer's worksite or premises for the duration of a semester or a summer and perform productive work, they should be paid at least the applicable minimum wage or consider eliminating the program altogether. Otherwise, there is a risk of inviting litigation or a DoL investigation.

As with all court-created rules and exemptions, there are no bright lines. There is a considerable distinction between an intern shadowing an employee for a week and an intern working full time for an employer for three months in the summer. Most internships fall somewhere in between. But, for employers who are convinced that the productive work performed by the intern is outweighed by the hassle in training and supervising the intern, recognize that such self-assurance is not immunization from legal attacks. Moreover, the DoL does not take a “balancing approach” in its Fact Sheet. Note that the Fact Sheet applies only to for-profit companies. Furthermore, the defendants in the lawsuits we examined in our research were for-profit employers. Therefore, if your company is a for-profit enterprise, do not hire interns without paying them at least the minimum wage. ✕

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¹U.S. DEP'T OF LABOR, FACT SHEET #71: INTERNSHIP PROGRAMS UNDER THE FAIR LABOR STANDARDS ACT (Apr. 2010), available at <http://www.dol.gov/whd/regs/compliance/whdfs71.pdf>.

² E.g., *Glatt v. Fox Searchlight Pictures, Inc.* No. 11 CV 6784 (S.D.N.Y. Sep. 28, 2011); *Wang v. Hearst Corp.*, No. 12 CV 00793 (S.D.N.Y. Feb. 1, 2012). “The Economist” reports more than 30 lawsuits in the U.S. involving former interns suing high-profile companies such as Sony, NBC, Donna Duran and the Pittsburgh Power. *Generation I*, THE ECONOMIST, September 6, 2014, at [].

³ See, e.g., Doris Meinert, *Fresh Faces*, HR MAGAZINE, November 2013, at 23 (stating that “Under U.S. Department of Labor rules, unpaid interns are trainees who aren't allowed to provide any services to a for-profit company. They can only observe.”). Also, the discovery in connection with the Fox Searchlight lawsuit revealed that the company believed that under the DoL regulations the Fox Searchlight internships had to be paid.

⁴ See, e.g., Defendant's Motion to Dismiss, *Wang v. Hearst Corp.*, No. 12 CV 00793 (S.D.N.Y. Feb. 1, 2012).

⁵ Opinion certifying class action, *Glatt v. Fox Searchlight Pictures, Inc.* No. 11 CV 6784 (S.D.N.Y. Sep. 28, 2011).

⁶ *See, e.g., id.*

⁷ Meinert, *supra* note 3, at 24.

⁸ *See* factor 6 of the Fact Sheet #71, requiring that both the employer and intern understand that the intern is not entitled to any wages. U.S. DEP'T OF LABOR, FACT SHEET #71: INTERNSHIP PROGRAMS UNDER THE FAIR LABOR STANDARDS ACT (Apr. 2010), available at <http://www.dol.gov/whd/regs/compliance/whdfs71.pdf>.

⁹ 29 U.S.C. §214(a) (2014).

¹⁰ *Generation i*, *ECONOMIST*, Sept. 6, 2014 at 10.

¹¹ 29 U.S.C. §206(a)(1) (2014).

¹² 330 U.S. 148 (1947).

¹³ *Id.*

¹⁴ *Id.* FLSA defines an “employee” as a person “employed by an employer,” a circular definition which has been left for courts to unwind. 29 U.S.C. §203(e)(1) (2014).

¹⁵ *Walling v. Portland Terminal*, 330 U.S. 148 (1947).

¹⁶ The six factor test used by the DoL is as follows: 1. The internship, even though it includes actual operation of the facilities of the employer, is similar to training which 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 existing staff; 4. 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; 5. The internship 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. U.S. DEP'T OF LABOR, FACT SHEET #71: INTERNSHIP PROGRAMS UNDER THE FAIR LABOR STANDARDS ACT (Apr. 2010), <http://www.dol.gov/whd/regs/compliance/whdfs71.pdf> (last visited November 12, 2014).

¹⁷ *See, e.g., Meinert, supra* Note 3.

¹⁸ *Glatt v. Fox Searchlight Pictures, Inc.* No. 11 CV 6784 (S.D.N.Y. Sep. 28, 2011). Note that the case is currently being reviewed by the Second Circuit. As of the writing of this article, no appeal decision has been published yet.

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Generation I*, *THE ECONOMIST*, September 6, 2014, at 10.

²² *Archie v. Grand Cent. P'ship*, 997 F. Supp. 504, 508 (S.D.N.Y. 1998).

²³ 29 U.S.C. §214(a) (2014). The same section also authorizes employment of “messengers of letters” at subminimum wage. Other exemptions to FLSA authorize employment at subminimum wages of full time students working at retail establishments (29 U.S.C. §214(b) (2014)) or employment of individuals with disabilities (29 U.S.C. §214(c) (2014)).

²⁴ 29 U.S.C. §214(c) (2014).

²⁵ 29 C.F.R. § 520.401 (2012).

²⁶ 29 C.F.R. § 520.404(d) (2012).

²⁷ *Id.*

²⁸ 29 C.F.R. § 520.403 (2012).

²⁹ The regulations allow for up to 240 hours to be paid at not less than 95% of the regular wage. The savings increase slightly when the employer working with the school applies through the “student-learner” route: the trainee may work up to one year at a subminimum wage no less than 75%.

³⁰ 29 C.F.R. § 520.408 (2012).

³¹ 29 C.F.R. § 520.506 (2012).

³² Under the Freedom of Information Act, the authors requested data from the DoL showing the applications for certificates under Sec. 14(a). The data is available on file with the authors. The certificates processed were all issued to employers employing what the regulations classify as “student learners.” The DoL has not issued any certificates to employers wishing to employ what the regulations classify as “learners” in the relevant time frame. The authors have not obtained data on certificates applicable to “apprentices,” (a category qualifying for Sec. 14(a) exemption), as it would be outside the scope of the article.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.*

³⁶ *Id.*

³⁷ *Walling v. Portland Terminal* 330 U.S. 148 (1947).

³⁸ NATIONAL ASSOCIATION OF COLLEGES AND EMPLOYERS, <http://nacweb.org/s06262013/unpaid-internship-FLSA-guidelines.aspx> (last visited November 12, 2014).

³⁹ *Id.*

⁴⁰ At least one other commentator reached similar conclusions. See Jessica Curiale, *America's New Glass Ceiling: Unpaid internships, the Fair Labor Standards Act, and the Urgent Need for Change*, 61 HASTINGS L.J. 1531 (July 2010).

⁴¹ Numerous companies have eliminated their internship programs in the aftermath of the DoL issuing the Fact Sheet, e.g. Conde Nest.

⁴² 29 C.F.R. 520.401(c) (2012).

⁴³ 29 C.F.R. 520.503(a) (2012).

⁴⁴ *See, e.g.*, 29 C.F.R. 520.403(a)(3), requiring a statement explaining why the employment “is needed to prevent curtailment of employment opportunities” or 29 C.F.R. 520.403(a)(8), asking for “straight-time average hourly earnings” of experienced workers in the learner occupations.

⁴⁵ Based on current federal minimum wage of \$7.25 and 40 hours of work required for earning 1 college credit (in addition to the academic component of the internship), a ratio typical at SUNY schools. (New York State's actual minimum wage is currently \$8.25.)