7 Employment Contracts Issues Facing DOL Scrutiny

By **Thomas Starks** (January 22, 2025)

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The U.S. Department of Labor released the fiscal year 2024 enforcement report in October, which focuses on contractual provisions that waive employees' legal rights or require worker payments to employers. The DOL's Office of the Solicitor has taken an aggressive approach in litigating these contractual issues.

In the past year, the solicitor of labor has taken a critical interest in employment contracts that include clauses limiting employee remedies or assigning employees contractual duties. These provisions range from requiring employees to waive statutory protections to enforcing penalties for leaving a job early.

While such provisions are increasingly common business practices, they sometimes violate federal labor laws, including the Fair Labor Standards Act, the Occupational Safety and Health Act, and the Employee Retirement Income Security Act.

The labor solicitor's report identifies seven types of provisions, each presenting a unique contractual clause. By including these clauses, employers seek to limit their liability while limiting employees' ability to take costly legal action. This article will address each category and highlight how the labor solicitor is taking steps to litigate their usage.

1. Waivers of Statutory Protections

One of the most prevalent issues is the inclusion of provisions that require workers to waive statutory rights, particularly under the FLSA. The FLSA guarantees workers minimum wage and overtime protections, and courts have consistently ruled that these rights cannot be waived by employment agreements.

Recently, contractual clauses have either shortened statutes of limitations for filing claims or barred recovery of liquidated damages — undermining remedies available under the FLSA.

In one recent case in the U.S. District Court for the Southern District of Indiana, Rodgers-Rouzier v. American Queen Steamboat Operating Co., the labor solicitor filed an amicus brief in 2023, opposing an arbitration agreement that also limited the time workers had to file wage claims.

The labor solicitor argued that shortened limitations periods may cause employees to waive recovery for FLSA violations. The court reinforced that such waivers undermine the public policy of protecting workers from substandard labor practices.

In a series of other cases, the labor solicitor made similar arguments against waiving statutory rights under ERISA. In those cases, some courts have adopted the labor solicitor position that arbitration agreements are unenforceable if they preclude employees from asserting planwide relief using ERISA, Section 502(a).

For example, in Cedeno v. Sasson, the U.S. Court of Appeals for the Second Circuit concluded on May 1 that the Federal Arbitration Act does not allow courts to enforce arbitration agreements that waive substantive statutory rights, in this case under ERISA

Section 502(a)(2). This is likely to be a continued area of litigation for the labor solicitor due to a circuit split on the issue.

This focus is significant because it highlights the tension between enforcing arbitration agreements and protecting workers' nonwaivable statutory rights under federal laws like the FLSA and ERISA.

In recent history, courts have consistently ruled that contractual provisions limiting workers' ability to assert these rights, such as shortening statutes of limitations or barring remedies, undermine public policy aimed at preventing exploitative labor practices.

This trend in rulings demonstrates the DOL's active role in challenging such provisions, emphasizing the broader importance of safeguarding minimum labor standards and ensuring access to planwide relief under ERISA.

The labor solicitor's proactive stance in litigating challenges to waivers of statutory protections may serve as a persuasive deterrent for attorneys contemplating the inclusion of such provisions in employment agreements.

Moreover, even when such waivers are present in an employment contract, defense counsel may exercise caution in invoking these provisions as a defense strategy to avoid drawing scrutiny from the labor solicitor.

2. Misclassification as Independent Contractors

Classifying workers as independent contractors is a common occurrence. Employers use it to limit legal responsibilities, such as paying overtime, providing health benefits, and paying Federal Insurance Contributions Act, or FICA, taxes.

However, many workers prefer to be classified as independent contractors to take advantage of tax deductions or to have greater control over their work. The DOL has made it clear that classifying workers as independent contractors does not exempt the employer from compliance with employment labor laws.

Earlier in 2024, the DOL issued a final rule that the economic realities test applies for determining classification as an employee or independent contractor for FLSA purposes. However, other federal agencies use different tests.

For example, the IRS uses the 20-factor test to determine if an employer sufficiently controls a worker enough to be labeled an employee. This can lead employers into a frustrating situation of having workers correctly classified as independent contractors with the IRS and incorrectly classified as independent contractors for FLSA purposes.

The labor solicitor has argued that contractual agreements that designate workers as independent contractors are not determinative under the FLSA. For instance, in a March brief filed with the U.S. Court of Appeals for the Fourth Circuit's Su v. Medical Staffing of America case, the labor solicitor contended that despite the nurses' contracts classifying them as independent contractors, the economic realities of the relationship indicated that they were employees entitled to FLSA protections. The labor solicitor has successfully made similar arguments in Occupational Safety and Health Administration cases.

The labor solicitor's arguing against the misclassification of independent contracts is significant because it underscores the legal and practical complexities surrounding worker

classification and the potential risks for employers who misclassify employees as independent contractors.

While many employers rely on independent contractor designations to limit legal and financial obligations, such as paying overtime and FICA taxes, the DOL has made clear that these designations do not exempt them from compliance with labor laws, particularly under the Fair Labor Standards Act.

For practitioners, the 2024 adoption of the economic realities test by the DOL for FLSA purposes creates a standard that may conflict with tests used by other agencies, like the IRS' 20-factor test, complicating compliance efforts.

Furthermore, the labor solicitor's position reinforces that contractual labels are not definitive; rather, the actual nature of the working relationship determines worker rights under the FLSA. This divergence increases the stakes for employers, as improper classification can lead to liability under multiple regulatory frameworks and heightened scrutiny by the labor solicitor in enforcement actions.

3. Indemnification Provisions

Indemnification clauses shift the cost of an employer's legal violations onto the employee. These provisions require workers to reimburse employers for legal expenses or damages related to employment disputes. The labor solicitor argues that these provisions discourage workers from filing complaints, as the financial risk is too great.

Federal courts have repeatedly ruled that employer indemnification clauses violate public policy. In a 2019 decision in Scalia v. MICA Contracting LLC, out of the U.S. District Court for the Southern District of Ohio, the labor solicitor argued that employers cannot shift FLSA liability to employees. The court agreed that allowing such clauses would weaken the incentive for employers to comply with labor laws.

The labor solicitor intervened in another private FLSA action arguing for the dismissal of a company's unjust enrichment counterclaim. In Provencher v. Bimbo Bakeries USA Inc., drivers filed an FLSA suit over misclassification, but they were countersued by their employer for unjust enrichment in an attempt to offset the back wages or liquidated damages.

In its 2023 decision, the U.S. District Court for the District of Vermont agreed with the labor solicitor that the unjust enrichment counterclaim should be viewed the same as an indemnification claim, thus not allowed under the FLSA.

The labor solicitor's stance on indemnification provisions is significant because it highlights the growing legal challenges to indemnification clauses that shift the financial burden of employer violations onto employees, a practice that undermines worker protections under the FLSA.

Such provisions deter workers from asserting their rights due to the financial risks involved, which conflicts with the public policy goals of the FLSA. Federal courts have consistently ruled that these clauses violate public policy by reducing employer accountability and weakening incentives for compliance with labor laws.

For practitioners, the labor solicitor's successful interventions underscore that indemnification clauses — whether expressly stated or framed as counterclaims such as

unjust enrichment — are impermissible and can result in increased litigation costs.

Counsel should be mindful that contractual provisions ordinarily enforceable in other contexts warrant heightened scrutiny in employment agreements, as employers cannot employ legal mechanisms to shift liability in a manner that undermines workers' rights or remedies. Such practices contravene the FLSA's protective objectives and may invite judicial invalidation or enforcement actions.

4. Loser Pays Provisions for Attorney Fees

So-called loser pays provisions in employment contracts provide that the losing party pays the attorney fees for the successful party. While the FLSA and many other employment actions include a one-way fee-shifting provision allowing employees to recover attorney fees if they prevail, these clauses seek to allow employers to be reimbursed if they successfully defend an action.

In a notable case, Su v. Advanced Care Staffing, out of the Eastern District of New York, the labor solicitor filed an amended complaint in 2023 for an injunction to prevent enforcement of the "loser pays" clause in a contract that required nurses to pay the company's legal fees in arbitration if the nurses left their jobs before completing a three-year commitment. The court sided with the labor solicitor and held that the recovery of attorney fees may be a type of kickback prohibited by the FLSA. This is because employers are not permitted to recover costs from employees when the cost is primarily for the employer's benefit.

This is significant because attempting to shift attorney fees onto employees if employers prevail in legal disputes cannot be done contractually. Such provisions conflict with the FLSA, which includes a one-way fee-shifting mechanism designed to incentivize employees to assert their rights without fear of financial retaliation.

The labor solicitor's position, underscores to attorneys that requiring employees to cover employers' legal fees can amount to an unlawful kickback under the FLSA. This ruling reinforces the principle that costs incurred primarily for the employer's benefit cannot be passed onto employees, safeguarding the FLSA's purpose of protecting workers from undue financial and legal burdens. For employment defense attorneys, one of the only remaining mechanisms to shift attorney fees to employees may be a Rule 68 offer of judgment.

5. Stay or Pay Provisions

"Stay or pay" provisions require employees to compensate their employer if they leave their job before fulfilling a specified term. The labor solicitor takes the position that this can keep employees in a job that has violations of worker protection laws by making it prohibitively expensive for them to leave. Examples of this include employers seeking compensation for the cost to replace workers, lost profits, attorney fees, and the cost of training provided to the employee. At times, these costs exceed what the employee was actually paid.

The labor solicitor has argued that such clauses violate the FLSA's "free and clear" wage payment requirement, which ensures that workers receive their wages without any strings attached. In the previously discussed Advanced Care Staffing case, the court ruled on May 8, 2024, that the labor solicitor presented a viable legal theory that the company's demand for reimbursement of lost profits and legal fees from departing nurses constituted an unlawful kickback that reduced the workers' wages below the statutory minimum provided by the FLSA.

Additionally, the FLSA forbids the repayment of costs that are primarily for the benefit of the employer. However, courts have sided with employers when the cost primarily benefits the employee, such as, employers paying for portable credentials including college degrees or police academy training.

For example, the U.S. Court of Appeals for the Seventh Circuit's 2002 ruling in Heder v. City of Two Rivers, Wisconsin, allowed the reimbursement of portable credentials, but declined to reimburse the employer for overtime incurred to attend the training.

The labor solicitor's stance on stay or pay provisions is significant because stay or pay provisions can effectively trap employees in jobs, even in environments with labor law violations, by imposing steep financial penalties for leaving before a specified term. Such clauses often require employees to reimburse employers for costs like training, lost profits, or attorney fees, sometimes exceeding the wages earned, which the labor solicitor argues violates the FLSA free and clear wage payment requirement.

Even if courts ultimately decline to enforce stay or pay provisions, employees may lack the legal sophistication to recognize the unenforceability of such clauses, leaving them feeling compelled to remain in substandard employment conditions.

For practitioners, the labor solicitor's position is significant because they should advise clients that some of their employer-incurred costs will not be reimbursed and attempts to be reimbursed can constitute an unlawful kickback if it reduces wages below the FLSA minimum.

While courts have sided with employers when the costs primarily benefit the employee — e.g., funding for portable credentials — the labor solicitor's success in challenging provisions benefiting employers underscores attorneys need to factor in the FLSA's focus on protecting workers from unfair financial burdens that undermine statutory wage protections.

6. Confidentiality, Nondisclosure, Nondisparagement Agreements

Confidentiality, nondisclosure and nondisparagement agreements have been a targeted enforcement area. This is because when they are broadly worded it can have an effect that prevents reporting violations or cooperating with government investigations. While NDAs can serve legitimate business purposes, overly broad provisions that restrict communication with labor enforcement agencies are unlawful, especially when accompanied by threats of monetary penalties or loss of employment.

The labor has acted against employers that use these agreements to prohibit employees from speaking with government investigators, require notification if contacted by government investigators, or prohibit discussing employment issues with co-workers.

For example, in July, the labor solicitor sought an injunction in the Eastern District of New York to prevent Smoothstack from enforcing provisions that could have chilled an employee's ability speak freely with the labor solicitor.

Smoothstack required employees to sign separation agreements with monetary fees for violating NDAs or confidentiality agreements. The labor solicitor alleges this is effectively retaliation against employees and prevents them from engaging in protected conduct under the FLSA.

In addition, the labor solicitor alleges this interferes with the DOL's authority under the FLSA

of investigation and enforcement.

The labor solicitor's targeting of these provisions is significant because overly broad confidentiality, NDAs, and nondisparagement agreements can undermine workers' rights and obstruct government enforcement of labor laws.

While NDAs can serve legitimate purposes, provisions that deter employees from reporting violations, cooperating with government investigations, or discussing workplace issues with co-workers violate the FLSA.

The labor solicitor's actions, especially in seeking an injunction, highlight that such agreements, particularly when coupled with monetary penalties or threats of employment loss, constitute retaliation and interfere with the DOL's investigatory and enforcement authority.

Attorneys need to be cautious because these provisions are common but require an attention to detail to specify that reporting violations and cooperating with government investigations are allowed under these agreements.

Practitioners need to take efforts to emphasize to their clients the importance of safeguarding employees' ability to engage in protected activities and ensuring employer compliance with labor laws.

7. Mandatory Reporting of Safety Concerns

Finally, some employers include clauses requiring workers to report safety concerns to the company before contacting government agencies like OSHA. The labor solicitor has taken the position that these provisions delay or obstruct the reporting of hazardous conditions, potentially endangering workers and violating OSHA regulations.

In Bakis v. Maersk Line Ltd. the labor solicitor argued before a DOL administrative law judge that the Seaman's Protection Act provided protection for employees from termination for reporting safety violations to the U.S. Coast Guard before notifying supervisors.

The labor solicitor's position was that seafarers have an unconditional right to report safety violations to the Coast Guard.

A settlement from the case requires Maersk to change its reporting policies and eliminate the need to first report to supervisors. The employee also received over $300,000 in back pay.

The labor solicitor has emphasized that workers have the right to report directly to OSHA or other worker safety organizations without first seeking their employer's approval. Contractual provisions to the contrary are unenforceable.

The labor solicitor's litigating workers' rights to report safety concerns directly to government agencies is significant because it underscores the importance of protecting workers' rights to report safety issues directly to government agencies like OSHA without obstruction from employer-imposed reporting requirements.

Clauses that mandate employees to first report safety issues to the employer before contacting regulatory bodies can delay or prevent timely reporting, potentially endangering workers and violating OSHA regulations. Effectively, this means employers do not have a

chance to correct safety issues before the government becomes involved.

For practitioners, the labor solicitor's position demonstrates its commitment to ensuring that employees, have an unconditional right to report safety violations to authorities, and that employer-imposed reporting restrictions are unlawful.

Attorneys should encourage corporate clients to make reporting safety issues to the employer as easy as possible, even anonymously, to encourage employees to first report concerns to the employer. The policy changes and significant back pay for the employee, highlights to practitioners the labor solicitor's priority in enforcing these protections.

Conclusion

The labor solicitor's 2024 enforcement report highlights a growing trend of enforcement against contractual provisions that limit workers' rights and avoid legal responsibility. Whether it is waivers of statutory protections, misclassification as independent contractors or indemnification clauses, the labor solicitor is aggressively litigating these employment practices.

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