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EMPLOYER RETALIATION

In employment decisions (as in comedy), CA case shows timing is everything

by Karen A. Henry
Davis Wright Tremaine LLP

It's a fairly common story: An employer disciplines or discharges an employee, who then files a lawsuit claiming the action is retaliation for a complaint or grievance she previously made ("protected conduct"). Although the employee's lawsuit describes a litany of "retaliatory" actions supposedly taken by the employer, the facts show large gaps of time between her alleged protected conduct and the employer's supposedly "retaliatory" actions.

Fortunately for employers, when the temporal proximity between an employee's alleged protected conduct and an employer's decision to discipline or discharge the individual is too attenuated, courts won't hesitate to dismiss the retaliation claim in the lawsuit's early stages. That is exactly what happened in the following case.

Saga begins

Aurora Le Mere began working as a teacher for the Los Angeles Unified School District (LAUSD) in 2002. Her 13-year career with the school district was storied, to say the least. For example, between July 2006 and February 2014, she filed numerous employment-related complaints, including:

- Two workers' compensation actions for injuries sustained when she was attacked by students;
- Two administrative complaints alleging the LAUSD violated provisions of the Education Code, one of which prompted an investigation by the Occupational Safety and Health Administration (OSHA);
- A civil action against the LAUSD and two individuals in 2007 alleging claims for discrimination, retaliation, and civil rights violations; and
- Seven years later, in 2014, a complaint against the school district filed with California's Department of Fair Employment and Housing (she subsequently received a right-to-sue letter).

Le Mere and the LAUSD settled her workers' compensation claims and the 2007 civil action, but the story didn't end there.

On February 10, 2015, Le Mere filed another lawsuit asserting the LAUSD had subjected her to "a pattern of continued harassment, intimidation, discrimination, hostility, and retaliation" because she engaged in "protected conduct"—i.e., filing her two workers' comp claims and the 2007 lawsuit against the school district. According to Le Mere, the district's treatment of her after she engaged in the protected conduct constituted unlawful retaliation in violation of Government Code Section 12940(h). Importantly, however, the

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allegedly unlawful conduct she attributed to the LAUSD occurred in 2006, 2009, and 2014.

The LAUSD asked the court to dismiss Le Mere's retaliation claim because she neglected to show a connection between her alleged protected conduct and the actions she attributed to the school district. The trial court agreed, and she appealed.

Retaliation claim requires proof of causal link

To prove a retaliation claim under Section 12940(h), the California Court of Appeal explained Le Mere had to establish (1) her engagement in protected activity, (2) retaliatory animus on the LAUSD's part, (3) an adverse action by the district, (4) a causal link between the retaliatory animus and the adverse action, (5) damages, and (6) causation. Of particular relevance here, the appellate court concluded she failed to establish causation, among other things.

It's all about the timing

While the court of appeal recognized that a close temporal proximity between an employee's protected activity and the alleged retaliatory conduct can raise an inference of causation, it also noted "several federal cases hold that intervals of more than a few months were too long to support causation." In Le Mere's case, nearly two years had elapsed between the 2007 lawsuit and the first alleged instances of retaliation in 2009. The court determined the two-year gap did not and could not prove causation.

Moreover, if the two-year gap was insufficient to prove causation, the seven-year gap between Le Mere's 2007 action and the conduct she attributed to the LAUSD in 2014 clearly was too attenuated to establish the required connection (the conduct she alleges occurred in 2006 obviously wasn't caused by a civil action she filed a year *later*). For that reason, the court concluded the trial court properly dismissed her retaliation claim.

Interestingly, Le Mere tried to avoid the dismissal of her retaliation claim by focusing on a notice of suspension she received from the LAUSD in August 2015. More specifically, in opposing the school district's request to dismiss the retaliation claim, she argued it issued the notice of suspension to retaliate against her for filing the *present lawsuit.* Her complaint, however, didn't include that theory of retaliation. Rather, as the court of appeal explained, her complaint based her retaliation claim on the *2007 lawsuit.*

Because Le Mere neglected to identify the 2015 notice of suspension in the complaint as one of the bases for her retaliation claim, the appellate court declined to consider it. In other words, the time to raise that belated theory of liability was when she filed her complaint, not when she was trying to salvage it. *Le Mere v. Los Angeles Unified School District* (California Court of Appeal, 2nd Appellate District, 4/30/19; published 5/14/19).

Bottom line

Clients contact HR professionals every day seeking advice about whether an employee's conduct warrants disciplinary action. HR pros are trained to get as much information as possible about the reasons a supervisor or manager is seeking to discipline an employee. In addition to asking questions about the specific events that caused the supervisor or manager to seek HR assistance, the *Le Mere* case reminds HR pros to dig deeper:

- Even assuming the supervisor or manager has articulated a legitimate basis for the contemplated disciplinary action, what else is going on with the employee?

- Has the employee recently submitted a work-related complaint or grievance?
- Has she notified the employer of a disability?
- Has she recently requested medical or personal leave?
- Has the employee recently been involved in a dispute with a coworker or supervisor?
- Is anything else going on in the employee's personal or work life that creates a risk the contemplated disciplinary action could be viewed as retaliatory?

Of course, the fact that an employee behaves badly in close temporal proximity to submitting a work-related complaint, requesting leave, or engaging in some other protected conduct doesn't mean the HR professional should advise the supervisor or manager to ignore the bad behavior. Before blessing a supervisor's request to discipline an employee, however, HR pros must make sure they're aware of any recent employment activity that may create or increase the risks for the employer.

Understanding the full scope of the relevant employment activities (including the temporal relationship between them) better positions HR professionals to make informed recommendations and, perhaps more important, to understand when to seek advice about the potential legal implications of any protected conduct that has preceded the contemplated disciplinary action. As the *Le Mere* decision demonstrates, the timing of an employment decision can mean everything!

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SETTLEMENT AGREEMENTS

CA Supreme Court provides clarity on offers to compromise in arbitration proceedings

by Cathleen S. Yonahara
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An offer to compromise under Code of Civil Procedure Section 998 incentivizes parties to settle. If a party rejects a pretrial offer to compromise and obtains a lesser result at trial, the opposing party may be awarded its costs. Section 998 applies to civil actions and arbitrations. The California Supreme Court recently issued a decision clarifying the deadline for requesting costs in arbitration proceedings under Section 998 and a court's authority to review an arbitrator's denial of costs.

Facts

In 2003, Shiraz Shivji, an engineer and inventor, retained attorney Alan Heimlich to represent him in a variety of intellectual property matters. The retainer agreement included an arbitration provision. In 2012, Heimlich sued Shivji for alleged failure to pay approximately $125,000 in legal fees. After a year of litigation, Shivji made a bid to settle the case under Section 998 for $30,001 and later offered $65,001. Heimlich rejected both offers.

Shivji asked the court to compel arbitration and stay (or put a hold on) further litigation, and it did so. In the arbitration proceeding, the engineer made a counterclaim for a refund of $176,000 for sums he already paid. Both parties requested costs.

On March 5, 2015, the arbitrator issued an award denying recovery to both parties and directing that "each side will bear their own attorneys' fees and costs." Six days later, Shivji notified the arbitrator of the two Section 998 offers to compromise and asked the arbitrator to award him costs since Heimlich had failed to obtain a more favorable result.

The arbitrator denied the request, stating, "Once I issued [my] Final Award I no longer [had] jurisdiction to take any further action in this matter. As discussed in the Award, whatever may have been costs, fees, etc. associated with the [court] litigation were to be borne by the parties and I didn't award either party attorneys' fees related to the arbitration."

Shivji then filed a request in the superior court to confirm the arbitration award and asked for $76,684.02 in costs. The court confirmed the arbitration award but denied the costs. The California Court of Appeal reversed, holding the engineer's postaward request for costs was timely and the superior court could vacate (or toss out) the arbitrator's award because the latter had refused to hear relevant evidence by summarily rejecting Shivji's attempt to raise the issue of costs.

Arbitrator has authority to allocate costs

Since arbitration is a matter of consent, the parties' agreement determines whether the arbitrator or the court has the authority to allocate costs. In the present case, the arbitration provision broadly provided that the parties agreed to arbitrate "all disputes or claims of any nature whatsoever." The provision was silent about the arbitrator's jurisdiction over ancillary matters, such as costs.

Under California case law, if the arbitration agreement doesn't limit the issues to be resolved through arbitration, the arbitrator is presumed to have authority to determine a party's entitlement to costs. Accordingly, the arbitrator had authority to determine whether Shivji was entitled to costs.

When evidence of Section 998 offer may be presented

A Section 998 offer must be made at least 10 days before the beginning of the trial or arbitration. If the offer is

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MARK'S IN-BOX

Predictability in the law after *Dynamex*—who knows?

by Mark I. Schickman
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We still don't know whether Governor Gavin Newsom will be a brake on California's Democratic legislature or a rubber stamp. The California Assembly's recent passage of **Assembly Bill (AB) 5** may provide an early test, once it passes the Senate—which it surely will.

AB 5 codifies the California Supreme Court's recent *Dynamex* decision and adds some wrinkles to it. By now, we all know that *Dynamex* abandoned the state's traditional common-law test for independent contractor status, a nuanced and multifaceted analysis. Instead, *Dynamex* uses a three-pronged pitchfork, which has the advantage of simplicity, if not accuracy. Under that blunt test, you are an employee unless all three of the following apply:

- The work performance is free from the hiring entity's control and direction;
- The work performed is outside the usual course of the hiring entity's business; and
- The worker regularly and customarily engages in the trade, occupation, or business.

California's Assembly just made the *Dynamex* test a state statute. While *Dynamex* interpreted only the state's wage orders, AB 5 more broadly applies to the definition of "employee" throughout the California Labor Code. As a statute, it also stands against the possibility that a future court may abandon *Dynamex* and restore the common-law test. AB 5 also preempts a competing bill that has been limping around Sacramento, which would have disapproved of *Dynamex* and restored the common-law test. That bill was dead on arrival.

Everybody recognized there were holes, gaps, and unintended consequences stemming from the *Dynamex* test; AB 5 corrected some, but not all, of them. Most important, AB 5 carves out a series of jobs from the *Dynamex* doctrine.

Under AB 5, licensed doctors, real estate agents, stockbrokers and financial advisers, direct salespeople, and hair stylists all remain subject to the common-law test, with some technical limitations. Similarly, professional service providers are kept under the common-law test if they meet yet another series of technical requirements.

Follow the bouncing ball

New amendments will likely be added to the legislation before it reaches the governor's desk, as some *Dynamex* anomalies aren't remedied by AB 5 as it stands. Everybody has their favorite example of an unreasonable and unfair application of the case. Mine is the traditionally independent contractor freelance journalist, with tons of discretion, working for many journals but, by definition, failing the middle prong of the test. It's hard to believe any legislation will catch all the continued glitches, but tweaks will keep coming as the lobbyists stay on AB 5 until it reaches the governor.

For us, whatever the legislation looks like, it will create a new world of compliance problems. We have been living with a common-law test of independent contractor status for decades, and—whether we like the test or not—at least we finally know what it is. Misclassifying an independent contractor carries serious ramifications, so being able to make the call accurately is quite important.

But all of our history determining independent contractor status goes out the window as new judicial and statutory tests have been created. None of the cases that have framed the issue in the past has any authoritative applicability, so we are all now somewhat at sea and making the determination of independent contractor status.

We will still begin our analysis by determining whether the individual is exercising independent discretion without extensive supervision. Importantly, if a worker does a job necessary for your operation that an outsider would assume is to be done by an employee, independent contractor status will be suspect. So the traditional role of an independent contractor filling in on a short-term basis to supplement your existing staff during the busy season may now be a thing of the past.

Finally, you're going to have to grill potential independent contractors about who their other clients are, how long they have been conducting business, and under what business form they operate. We don't know how the California Labor Commission—or the courts—will interpret the test's language.

On all the points, until we get new guidance, nobody can be sure how the rules will be applied. That is troubling when predictability and consistency are what we look for in employment rules. After decades of grappling with, and perhaps finally understanding,

the common-law test, that history is now out the window, at least until the courts and the legislature decide to change the rules again.

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declined or not accepted in a timely fashion, it is deemed to have been withdrawn and cannot be used as evidence during a trial or arbitration to prove liability. Shivji argued the above restriction on admissibility prevented him from seeking costs until after the arbitrator issued an award because he was barred until then from telling the arbitrator about his settlement offers.

The California Supreme Court disagreed, holding that although a Section 998 offer is inadmissible to prove liability, it may be submitted to prove unrelated matters. Thus, Shivji wasn't prohibited from advising the arbitrator of the rejected Section 998 offer before the award.

In contrast, Heimlich argued that a preaward request for costs is mandatory because the arbitrator loses all jurisdiction after an award. The supreme court disagreed with him as well. Simply because Shivji could have raised the rejected Section 998 offer sooner doesn't mean he was required to do so.

Section 998 provides a time frame for when a compromise offer may be made and accepted, but it doesn't address when a request for costs must be made. In court cases, that timing is governed by California Rules of Court, rule 3.1700, which provides that a party seeking costs must file a memorandum within (1) 15 days of notice of entry of judgment or (2) 180 days of entry of judgment in the absence of a notice.

The supreme court held that consistent with civil litigation cases, 15 days after issuance of a final award, a party to an arbitration may submit a cost request based on the opposing party's rejection of a Section 998 offer. The arbitrator has implicit power under the section to consider the request and amend any award accordingly.

Arbitrator's denial of costs cannot be thrown out

Although Shivji's request for costs was timely, the high court determined he wasn't entitled to judicial relief. A court's power to correct or throw out an erroneous arbitration award is narrowly circumscribed. Such an award may be vacated only for fraud, corruption, misconduct, an undisclosed conflict, or similar circumstances involving serious problems with the award itself or with the fairness of the arbitration process.

In the present case, the arbitrator refused to consider Shivji's request for costs because he incorrectly believed he lacked jurisdiction. Under California law, however, an arbitrator's legal error in failing to award costs to a qualifying party under Section 998 isn't grounds for relief. Accordingly, the supreme court reversed the court of appeal's judgment with directions to affirm the trial court's confirmation of the arbitration award and denial of costs. *Heimlich v. Shivji* (California Supreme Court, 5/30/19).

Bottom line

The high court's *Heimlich* decision provides welcomed clarity about the timing requirements for requesting an award of costs following a rejected Section 998 offer to compromise in arbitration proceedings. If a party makes a compromise offer under Section 998 and the opponent rejects it and obtains a less favorable result at trial or arbitration, then within 15 days of the judgment or arbitration award, the party who made the offer may request an award of costs.

Furthermore, the case highlights the extremely narrow grounds on which a party may appeal or modify an arbitration award. Although the arbitrator erroneously denied Shivji's request for costs, those kinds of legal error aren't grounds for granting relief from the arbitrator's decision.

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PENSIONS

CalPERS pensions: when 'special compensation' isn't so special

by Mathew A. Goodin
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California Public Employees' Retirement System (CalPERS) is regularly called on to determine whether certain compensation earned by public employees is properly included in calculating their future pension rate. Generally, an employee's pension rate is based on his regular rate of pay and doesn't include extra compensation, such as overtime. The following case looks at whether an employee's bonuses, earned over six years, were properly included in calculating his pension rate. The outcome turned on whether the bonus payments were "special compensation" as defined by the Government Code.

Is consultant's $1.2M bonus included in pension benefit?

The Department of Social Services (DSS) is a state agency responsible for determining the medical

eligibility of disabled Californians who are seeking federal Social Security benefits or state Medi-Cal benefits. Dr. Robert Paxton is a medical consultant-psychiatrist who was responsible for reviewing claims involving psychiatric issues. Medical consultants are expected to (1) be at work during the "core hours" of 9:00 a.m. to 11:30 a.m. and from 1:30 p.m. to 2:30 p.m. and (2) average 40 hours per week. Otherwise, they have flexibility to decide when they work.

The DSS has historically suffered from periodic backlogs of cases and, in 1993, received a temporary exemption from the Department of Personnel Administration (now the Department of Human Resources) allowing the DSS to pay overtime to consultants even though they were properly exempt as "professionals" from federal and state overtime requirements. After a second requested exemption was denied in 1996, the DSS and the union representing the consultants ultimately agreed on a bonus program paying them for each case closed above a certain threshold per week.

Paxton was able to earn significant bonuses while participating in the bonus program from 2005 until it ended in 2011, even though he claimed he didn't work more than 40 hours per week. He said computerization of the records allowed him to review a case in an average of only five minutes. At that rate, he was able to pass the threshold of 90 cases in about a day and earned monthly bonuses ranging from $16,821 to $39,501 and totaling more than $1.2 million.

From 2003 to 2011, members of CalPERS were allowed to purchase additional years of retirement service credit. Under the program, an employee paid the present value of the increase in his pension benefit that would result from the purchased additional service credit. When CalPERS calculated that Paxton's cost to purchase additional retirement service credit would be based on a rate that didn't include his bonuses, he appealed.

An administrative law judge issued a proposed decision that the bonuses didn't qualify as "special compensation" and were therefore not includable in Paxton's pension. The CalPERS board adopted the decision with minor changes. The doctor then filed a writ under a provision of the Code of Civil Procedure that provides for trial court review of decisions by administrative agencies such as CalPERS. The trial court denied the petition, and he again appealed.

Bonus may or may not be 'special compensation'

The issue for the California Court of Appeal was whether the trial court erred in concluding the bonuses weren't special compensation that must be included when calculating an employee's pension benefit. What is "special compensation"?

- Government Code Section 20636 defines "special compensation" as "compensation for performing normally required duties" and provides examples such as holiday pay, hazard pay, and bonuses for duties performed on regular work shifts.
- The same section excludes "compensation for additional services outside regular duties" and provides similar examples such as standby pay, callback pay, court duty, and "bonuses for duties performed after the member's regular work shift." Overtime also isn't included as "special compensation."

Paxton argued the bonuses were pensionable because they were earned during his regular shift and he didn't work overtime to earn them. But the appellate court focused instead on whether they were earned for work that was part of his regular duties. The court concluded a bonus earned for purely voluntary services performed outside an employee's duties isn't special compensation, regardless of the time frame in which it was earned.

In looking at the bonus program's history, the appellate court relied on the fact that it was a replacement for an overtime program, and the union had taken the position that the extra work deserved extra compensation because it wasn't part of the consultants' regular duties. In other words, the extra pay wasn't pensionable compensation because it was intended to compensate Paxton for performing additional work outside his regular duties even if, for whatever reason, he was able to complete the work within his normal 40-hour workweek. *Paxton v. Bd. of Admin, CalPERS* (California Court of Appeal, 3rd Appellate District, May 20, 2019).

Bottom line

Soaring pension and overtime costs are a continuing hot-button topic in California and elsewhere. Indeed, the funding for the DSS bonus program at issue in this case was stopped by the federal government in November 2011 after news reports exposed the amount of the bonus payments.

Because the payments were clearly meant to be a replacement for overtime, the court of appeal's decision seems correct. While Paxton may not be happy, California taxpayers can take some solace in knowing he and the other DSS consultants won't be allowed to double-dip on the state's dime.

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WAGE AND HOUR LAW

Shifting attorneys' fees is dead end for employers, CA appeallate court says

by James S. Brown and Heather J. Zacharia
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On May 24, 2019, the California Court of Appeal decided an employer isn't entitled to attorneys' fees even when it prevails on a wage claim that's "inextricably intertwined" with a valid contractual claim for the fees. State courts are consistent in using public policy to justify preventing employers from recovering attorneys' fees when they prevail on claims against current or former employees. The following case continues that trend.

Shifty executives

In the 1980s, Nessim Bodokh and David Haccoun founded Dane-Elec Memory; the pair later formed Dane Corp. Bodokh was the CEO, and he and Haccoun were the company's board of directors. Bodokh, who is a citizen and resident of France, doesn't have a U.S. work visa. Dane Corp. treated him as an independent contractor and paid him "executive compensation" by wire transfer directly to his business account. Nothing was withheld from his pay for federal, state, or French income taxes.

Sometime in 2007 or 2008, Bodokh discovered an investment opportunity requiring a $500,000 investment each from Bodokh and Haccoun. The pair received corporate loans from Dane Corp., which were documented by promissory notes. The board (Bodokh and Haccoun) approved the loans, totaling $1 million, and the board's minutes included a resolution authorizing them.

In December 2009, Dane Corp. received an initial distribution of more than $13.9 million from a class action settlement. At a December 28 meeting, the board of directors (Bodokh and Haccoun) agreed to compensate Bodokh with a one-time bonus of $1 million, from which $400,000 was used to pay down the promissory note, leaving a remaining balance of $100,000, payable in installments beginning in September 2010.

Bodokh made none of the payments. In 2012, a renewed promissory note was made to reflect the $100,000 balance he owed. He then made no payments on the renewed promissory note.

Beginning in 2009, Dane Corp. and its wholly owned subsidiary, Dane Memory, suffered financial difficulties. As a consequence, and at Bodokh's direction, the company:

- Implemented a payment reduction plan (PRP) requiring all *salaried* employees to accept a pay reduction until the company made a profit, at which time they would be paid retroactively; and
- Reduced Bodokh's monthly compensation to $6,700.

A September 2011 conciliation agreement between Dane Memory and its creditors indicated Bodokh had agreed to reduce his monthly compensation to $6,700 gross, not net. Later communications between the company's chief financial officer and its controller confirmed Bodokh's compensation during the PRP was $6,700 gross. Dane Corp.'s general counsel sent an e-mail indicating her belief Bodokh's compensation under the PRP was net, not gross, but the company didn't adjust his compensation since doing so would have conflicted with the conciliation agreement.

In 2014, Dane Corp. recovered financially and paid its remaining employees their withheld wages, plus 10 percent interest, and restored their salaries to pre-PRP levels. Employees who had voluntarily left the company weren't paid.

The road to attorneys' fees

Dane Corp. filed suit against Bodokh for breach of the second renewed promissory note. He cross-claimed against the company for failing to pay wages and committing waiting-time penalties under Labor Code Section 203, based on the failure to "gross up" the $6,700 for taxes or pay the reduced compensation differential after the business became profitable. The trial court found in Dane Corp.'s favor on both the complaint and the cross-complaint.

Dane Corp. filed a request for attorneys' fees in the amount of $59,637, based on a provision in the second renewed promissory note allowing attorneys' fees to the prevailing party. The trial court granted the employer's motion and awarded it fees of $50,959.50, but it disallowed $8,677.50 in attorneys' fees that it viewed as relating solely to Bodokh's wage claim.

It's a one-way street

Labor Code Section 218.5 is a fee-shifting statute in actions for nonpayment of wages. It awards attorneys' fees and costs to the prevailing party in an action for nonpayment of wages. If the winning party is "not an employee," however, the fees and costs can be awarded only if the court finds the employee filed the court action in bad faith. The issue on appeal was whether an

employer could recover attorneys' fees incurred in successfully defending a wage claim, not filed in bad faith, when it was "inextricably intertwined" with a contract claim through which the employer would otherwise be contractually entitled to recover the fees.

In a win for employees, the court of appeal held that unless the trial court finds bad faith, Section 218.5 precludes an award of attorneys' fees to an employer that not only successfully defended the wage claim but also has a contractual right against the employee for the fees. Substantial evidence supported the trial court's finding that Bodokh had breached the second renewed promissory note by making no payments on it.

Bodokh wasn't a salaried employee and therefore wasn't entitled to retroactive wages after Dane Corp. became profitable. The conciliation agreement referred to a reduction in his "compensation," not "salary." Dane Corp. never withheld taxes from his compensation, and all evidence pointed to his reduced salary being gross, not net. The parties didn't dispute that Dane Corp. has a contractual right to attorneys' fees and costs incurred in enforcing the second renewed promissory note.

The general rule is that attorneys' fees don't need to be apportioned when they relate to an issue common to both a cause of action (or claim) in which a fee award is proper and one in which it isn't allowed or when it would be impossible to separate the attorneys' time into compensable and noncompensable categories. In this case, however, the fundamental public policy underlying the statutory right in favor of employee (not employer) recovery requires a different result.

The court of appeal determined it would frustrate the legislature's purpose in enacting Section 218.5 to turn a unilateral fee-shifting statute (if there is no bad faith) into a reciprocal one despite the contractual right to recover attorneys' fees. When "important" public policy requires it, a specific fee-shifting statute will control over a contractual provision allowing attorneys' fees or costs to a prevailing party. *Dane-Elec Corporation, USA v. Nessim Bodokh* (California Court of Appeal, 4th Appellate District, 5/24/2019).

Bottom line

It isn't news to anyone operating a business in California that the wage and hour laws plainly favor employees. Their enforcement is driven largely by employee-initiated actions, and it appears to be sacrosanct that there should be no hint of any chilling effect on encouraging employees to assert their rights. Separate contracts with certain employees, such as the executive in this case, on nonwage subjects should still allow for prevailing parties' fees and costs. However, you should be cautioned that it's easier for an employee to dispute that right than it is for an employer to enforce such a recovery.

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WORKER CLASSIFICATION

When determining contractor status, ABC test applies retroactively

The U.S. 9th Circuit Court of Appeals (whose rulings apply to all California employers) recently ruled the California Supreme Court's 2018 Dynamex decision, which adopted the "ABC" test to determine whether a worker is an employee or an independent contractor, applies retroactively to claims that arose years ago, when individual franchisees claimed their national franchisor was their employer under state law.

Background

Jan-Pro Franchising International advertises itself as being in the commercial cleaning business. It does not, however, directly employ workers who perform cleaning services. Instead, it operates under a "franchise" model in which it contracts with regional franchisees and sells them the exclusive right to use the Jan-Pro trademarked logo in a defined geographic area.

Like Jan-Pro, the regional franchisees don't provide cleaning services directly to customers. Instead, they contract with individual workers to do that. Thus, the business arrangement is a three-level structure, with Jan-Pro at the top, the regional franchisees in the middle, and the individual workers at the bottom. The individual workers are treated as franchisees of the regional franchisees and are characterized as independent contractors.

Three workers—Gerardo Vazquez, Gloria Roman, and Juan Aguilar—sued Jan-Pro for violating California's minimum wage and overtime laws. They asserted that despite the franchise structure, they were employees and Jan-Pro was their employer under state law. The trial court rejected the workers' claims, and they appealed to the 9th Circuit.

While the case was pending before the 9th Circuit, the California Supreme Court issued its decision in *Dynamex Ops. W. Inc. v. Superior Court* and adopted the ABC test to determine whether a worker is an independent contractor or an employee under California's wage and hour laws.

The central issue presented to the 9th Circuit was whether the ruling in *Dynamex* should be applied only prospectively to cases arising after the decision was issued or whether it should be applied retroactively to all cases. The court ruled it should be applied retroactively.

What is the ABC test?

Under California wage and hour law, for a worker to be considered an employee, the putative employer (the "hiring entity") must "suffer or permit" the person to work. *Dynamex* clarified that requirement by concluding

a hiring entity will be considered the worker's employer unless it can prove three things:

(A) The work performance is free from its control and direction;

(B) The work performed is outside the usual course of its business; and

(C) The worker regularly and customarily engages in that occupation or business.

The hiring entity must prove all three elements to avoid employment status. As the California court remarked, that's an exceptionally broad standard.

Was Jan-Pro the 'employer'?

We don't know for sure yet because the 9th Circuit sent the case back to the trial court to develop the facts necessary to apply the ABC test. The court did, however, provide "guidance" to the trial court.

First, the fact that this case involves a franchise structure doesn't make any difference. The ABC test applies to franchises just as it does to other businesses. In fact, the court noted that at least one court in Massachusetts has applied it to find the top-level franchisor was the employer of the bottom-level franchisees in a structure very similar to Jan-Pro's.

Second, the "B" prong of the test may be the easiest to apply. The prong requires the hiring entity to prove it isn't engaged in the same usual course of business as the worker. In applying Prong B, courts generally have considered three questions:

(1) Was the work necessary to or merely incidental to the work of the hiring entity?

(2) Was the work continuously performed for the hiring entity?

(3) What business does the hiring entity proclaim to be in?

Although the 9th Circuit didn't tell the trial court how it should answer those questions, it did make some observations that seem to indicate its preliminary impressions:

- Jan-Pro's business depends on someone performing the cleaning, and because it receives a portion of customers' payments, it actively and continuously benefits from the work.
- Its business model relies on the workers continuously performing the cleaning work.
- It holds itself out as a commercial cleaning company that provides cleaning services—not simply a business that "franchises."

What about regional franchisees?

The workers didn't sue the regional franchisees, perhaps because the agreements between them required claims to be arbitrated. It's apparent from the 9th Circuit's decision, however, that the regional franchisees are even more likely to be deemed employers because of their direct relationship with the workers. They also provide the workers their initial book of business as well as startup equipment and cleaning supplies, training, and assistance with customer relations. *Vazquez v. Jan-Pro Franchising International,* Case No. 17-16096 (9th Circuit, May 2, 2019).

Takeaways for employers

The significance of this decision extends far beyond the franchise industry. The retroactive application of the ABC test exposes all businesses in California that rely on independent contractors to provide the services they sell—a common feature in the "gig" industry.

Of course, this also is an important decision for the franchise industry in other states that apply the ABC test to determine employee status. Because franchisors will be evaluated under the same worker-friendly test as other businesses, they will be at increased risk of being liable for wage and hour violations.

The decision also serves as a reminder that even in states that haven't adopted the ABC test, it isn't uncommon for state workers' compensation and unemployment compensation laws to use a similar definition of "employment" to impose payroll taxes on employing entities for the work of independent contractors. Many of the states actively enforce those laws to increase their payroll tax revenues. ✤

WAGE AND HOUR LAW

What to do when U.S. DOL comes knocking at your door

The U.S. Department of Labor (DOL) performs wage and hour audits of employers by selecting them at random, or because they are in targeted industries (usually low-wage), or as a result of a complaint from an employee or former employee. The investigations have increased significantly over the past few years and can result in orders for back wages and penalties. What steps should you take when the DOL comes knocking (generally with no prior notice)? Read on and you'll learn!

Be prepared to cooperate

The DOL may send a letter at the start of an audit and ask for a variety of documentation to perform a "desk audit," which means they will likely not come into your place of business. You *must* provide all documentation sought or negotiate a compromise about what will be produced. If you don't reach a compromise or produce the documents requested, the DOL can obtain a subpoena forcing you to produce them. This usually results in the auditor characterizing the employer as uncooperative, which can result in more aggressive enforcement, including back wages, liquidated damages,

"willful" findings, and civil monetary penalties. At that point, you've lost your ability to negotiate for less or easier-to-produce data.

The DOL doesn't always initiate an audit with a letter request for information. Sometimes, an agency investigator will show up unannounced on your doorstep and ask to start looking at data and interviewing witnesses. How do you deal with these potentially costly, disruptive investigations and requests for detailed pay information? Here's how.

Step 1: Immediately call your employment legal counsel. They will know the process and can provide privileged legal and strategic advice. They may know the auditor and be able to provide useful information on the auditor's "style." Your counsel can also help you negotiate a narrower data production than initially requested and get a deadline extension if needed. They can also fill you in on what to expect and where you can "push back." To reduce your stress, you can request that the agency go through your counsel for everything related to the audit. The auditors are used to this and won't think you are trying to hide something.

Step 2: Analyze the documentation request. Is it overly burdensome? It always looks that way but often is not. Get your payroll service involved in responding to the requests. Provide the information in a useful format, preferably electronic, that the auditor can easily examine. If documents truly don't exist or are nearly impossible to provide, explain why and negotiate for alternative information or a format that is easier to obtain. Proposing a narrower scope, if there's a rational reason, can be successful. The more cooperative you are, the less likely it is that the auditor will insist on a personal visit, disrupting your workplace.

Step 3: If the DOL shows up on your doorstep without notice, you do *not* have to let them in—at least

CALIFORNIA NEWS IN BRIEF

Wage theft citations issued over failure to pay construction workers. The state labor commissioner's office announced on May 29 it had issued citations totaling $597,933 in unpaid wages and penalties to Universal Structural Building Corp. of Chatsworth after 62 construction workers were never paid for weeks of work on two projects in Hollywood and Ventura. J.H. McCormick Inc., a general contractor for one project, was named jointly and severally responsible for $68,657 of the citations under a section of the California Labor Code that holds general contractors liable for their subcontractor's wage theft violations.

$150,000 settlement reached in sexual harassment suit. The California Department of Fair Employment and Housing (DFEH) reported on May 22 that it had reached a settlement in a sexual harassment lawsuit filed on behalf of four women farmworkers against Canal Farms, the L.C. Dennis Company, Inc., a Canal Farms foreman, and a farm labor contractor. In addition to providing a $150,000 monetary settlement, Canal Farms will update its discrimination policies, provide harassment prevention training, and report to DFEH all internal complaints of discrimination for a three-year period. The civil complaint (Colusa County Superior Court case number CV24272) alleged that from early 2014 to October 2016, a Canal Farms foreman sexually harassed four women workers with constant crude and demeaning sexualized remarks, creating an intolerable work environment.

Companies settle EEOC disability lawsuit. Time Warner Cable, Inc., and Charter Communications, Inc., in May agreed to pay $99,500 to settle a disability discrimination lawsuit filed by the Equal Employment Opportunity Commission (EEOC). The suit was filed at the U.S. District Court for the Central District of California. The suit claimed an employee requiring a leave of absence for surgery to remove a cancerous nodule from her thyroid was fired while she was recovering from surgery—10 days after the surgery and three weeks before she was set to return to work. The EEOC charged that Time Warner failed to provide the employee with a reasonable accommodation of leave for her disability and instead unlawfully terminated her despite knowing she had undergone potentially lifesaving surgery to remove the cancerous nodule and was recovering.

DOL investigation results in restaurant paying back wages, damages. O-Fire Corp., operating as Onami Seafood Buffet in San Diego, will pay $29,992 in back wages and liquidated damages to two employees after a U.S. Department of Labor's (DOL) Wage and Hour Division investigation found violations of the overtime and record-keeping provisions of the Fair Labor Standards Act (FLSA). Investigators found the employer failed to pay two cooks overtime when they worked more than 40 hours in a workweek. Instead, they were paid flat salaries without regard to the number of hours they worked. The employees worked an average of 52 hours per week. The employer also violated the record-keeping requirements of the FLSA when it failed to accurately record the total number of hours employees actually worked, the DOL said. ✤

not that day. Especially if you have a legitimate reason that the audit will not be effective that day, a delay may be acceptable. Operational issues such as a major project or product deadline that day or week, a customer visit that prevents staff from being available, inability to access the data that day or in the preferred format, and absent staff who are necessary for the audit are all valid reasons to propose a delay. On the other hand, if you can make time and have some data available, offer it up and cooperate as much as possible. Offer to reschedule the visit so you can be prepared at a more convenient time, or you can often arrange to provide the information to the auditor in electronic or other more convenient format than is available that day. This may preclude the need for a potentially disruptive site visit.

Step 4: Proactively do your own audit of wage and hour issues. To prevent the self-audit from being accessible by the DOL or a private attorney, it should be done within the framework of the attorney-client privilege, which requires a letter from your counsel and some direction. Cross-check pay records to ensure that all employees have been paid for all time worked. Look for discrepancies in time records vs. hours paid and changed or missed punches, especially if the changes were done by supervisors and not the employee. Have hours been "automatically" reduced by assumptions that all workers took a meal break every day? Ensure that employees are properly classified as exempt or nonexempt. Check to see if salaries for exempt employees haven't been improperly reduced for missed partial days. Do you have independent contractors who legally do not qualify for contractor status and should be employees? These are all items the DOL will investigate, and you should know the answers before the agency shows up. If you find problems, fix them before the audit or let the auditor know you are in the process of doing so.

Step 5: Be diplomatic. Apologize for any missing information or delay in providing data. Do not stonewall, and avoid being antagonistic or hostile.

Step 6: Cooperate with witness interview requests. If the DOL wants to interview employees, it's in your best interest to help set them up on your premises so you know who is being interviewed and can prepare them on what may be asked. The auditor may work with you but not always. Some auditors will request a list of all employees with home contact information to reach them during off-work hours. They will interview a random selection of types of employees, and you won't know who's being selected. You may need to explain to all employees what's going on and that they may be interviewed but are free to accept or decline. Most employees are nervous and reluctant to participate in interviews. They may want counsel present, and you certainly can provide them with counsel. However, the DOL will often refuse such arrangements, and you cannot compel them to allow counsel to be present unless it's a manager or supervisor. Counsel can and should be present for any management interviews—insist on it. It's your legal right, even if the auditor tries to tell you it isn't allowed or needed. Everyone interviewed should ask for a copy of their statement, and then hopefully they will agree to share it with management or counsel. There's no reason you cannot debrief witnesses, as long as they cooperate voluntarily with you.

Bottom line

Follow these steps, and you'll have a much better chance of resolving the DOL audit successfully without back wages, liquidated damages, a third year of liability, or civil monetary penalties being assessed. ✤

WORKPLACE ISSUES

It's not me—it's you: how to break up with your employees

Relationships—both personal and professional—can be complicated. Just like first dates, job interviews offer candidates the chance to show a prospective employer the best possible version of themselves: smart, charming, funny, and responsible. As an employer, you ask exploratory questions about a candidate's background, education, interests, and goals for the future to see if it's a good fit. If you both agree that it is, you start a relationship.

Breakup options abound

Sometimes, it's a perfect match. Other times, the relationship isn't as great as you had hoped, and the employee reveals his true self: not smart, not that charming, not that funny, and somewhat irresponsible. In personal relationships, you have a few options for a breakup: You can ghost the other person, send him a text message, meet face-to-face and say, "It's not you—it's me," or have an open, honest dialogue about why you think it's best to end the relationship.

We have seen situations in which employers, rather than taking the "open, honest dialogue" approach, treat their employees unprofessionally and lack any compassion when terminating workers' employment. Some choose to announce terminations via e-mail. Others choose not to tell their employees while they are out on approved medical leave that their employment has been terminated—no call, no letter, no text message, nothing. Such behavior reflects poorly on the organization and leaves the door wide open for a lawsuit.

Treat employees as well on the way out as on the way in

A termination is humbling, even when it's deserved. Blindsiding employees with a discharge will inspire

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them to seek revenge on social media and in the courtroom. Your employees are an extension of your public relations department. By treating them as well on their way out as you do on their way in, you can prevent embarrassing viral posts and lawsuits. But that's a bonus, not the point.

As a supervisor, you have the responsibility to treat your employees with dignity and respect. While you may not enjoy confrontation, you can fire a poor performer with civility. To do that, you have to accept that no one—from the janitor to the CEO—is perfect. Employees' strengths and weaknesses stand out in different roles and areas. Alert your employees to any issues with their performance as they occur, and treat all employees equally—and document your actions. Praise in public, criticize in private, and consistently give honest and specific performance evaluations.

Ask poor performers, 'Are you happy?'

If an employee continues to fall short in one or more areas, meet with her privately, and ask a simple question: Are you happy with your job? If the answer is no, the solution is equally simple: Discuss whether the job is right for her. If the answer is yes, work with her to determine the reason behind her poor performance, outline areas for improvement, and provide a timeline to improve. If possible, provide metrics and objective expectations.

If, after a few weeks, the employee hasn't made progress, try finding open positions in your organization that could be a good fit. If none is available, schedule an in-person meeting, even if it requires you to travel. Kindly and directly frame the issue as a situation where the employee isn't the best match for this particular job, list her strongest attributes, and encourage her to pursue a role that better fits her skill set and passion. If attendance and timeliness are an issue, suggest jobs that have flexible schedules. Empower the employee to find a job she'll love.

Bottom line

You have the power to make the employment relationship a positive one or a negative one—right through to the end. Wield it wisely. ✤