employment brief

Legal Developments Affecting Employers
Murchison & Cumming, LLP Management Advisors

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CONTENTS

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Costs for Misclassification of Independent Contractors Worsen

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Stiff Penalties and Public Notice for "Willful" Misclassification

Misclassification of workers as "independent contractors" has long held grave consequences for employers. Liability for back pay such as overtime and missed meal premiums, benefits which would have been paid under an employee classification, as well as a mandatory award of attorney's fees to a prevailing plaintiff, have made misclassification cases shark bait for the plaintiff's bar in the wage and hour field.

Beginning on January 1, the consequences for misclassification become yet more draconian, as two new statutes have been added to the California *Labor Code* imposing stiff penalties on employers who "*willfully*" misclassify employees as independent contractors.

> **"Penalties begin at $5,000 for each violation and are in addition to penalties available under other statutes."**

According to the statute, "'*Willful misclassification' means avoiding employee status for an individual by voluntarily and knowingly misclassifying that individual as an independent contractor.*"

The penalties are set forth in *Labor Code* § 226.8, and amount to:

- $5,000 (minimum) to $15,000 (maximum) "for each violation."

- $10,000 (minimum) to $25,000 (maximum) "for each violation" if the employer is found to be "engaging in a pattern or practice of these violations."

Further, these penalties will be available in addition to any other penalties which might be sought against an employer, for example under the Private Attorneys General Act ("PAGA"), Labor Code § 2699, whereby an employee can seek to recover penalties on behalf of other "aggrieved" employees in the amount of $100 per pay period for a first violation and $200 per pay period for subsequent violations.

The new penalties could be imposed by either a court, such as in a wage lawsuit, or by the Labor and Workforce Development Agency, under the state's authority to investigate complaints of wage and hour violations. The statute also authorizes their assessment for individual wage actions brought to the Labor Commissioner under *Labor Code* § 98.

The statute also prohibits an employer from charging a "willfully misclassified" independent contractor any fees or expenses.

Beyond Penalties – Public Notice of Violation:

The new law goes beyond a pile-on of penalties. In fact, the legislature has taken the unusual step of requiring an employer to post "*prominently on its Internet Web site*" the fact that it has been found to have "*committed a serious violation of the law by engaging in the willful misclassification of employees*." If the employer does not have a website, then the notice must be displayed "*prominently*" in an area accessible to employees and the public. Further, the notice must advise employees how to contact the Labor Workforce Development Agency if they believe they have been misclassified.

Joint and Several Liability for Knowing Advice to Avoid Employee Status:

A related statute effective on January 1, 2012, will impose joint and several liability on any person "*who for money or other valuable consideration knowingly advises an employer to treat an individual as an independent contractor to avoid employee status for that individual.*" (*Labor Code* § 2753.) However, the statute excludes such liability to those who provide advice to their employer (e.g., human resources professionals) and attorneys providing advice in the course of their practice.

Unanswered Questions:

The meaning of "willfulness" is sure to be a battleground for future construction by the courts, as willfulness in other contexts in employment cases does not always require a wrongful intent. However, since the statute requires "willful misclassification," the straightforward construction would suggest a knowing decision to misclassify.

The meaning of a "pattern or practice" of violations – which raises the minimum penalty from $5,000 to $10,000 for a single violation -- is another foreseeable area for battle.

The statute offers no framework for the amount of the penalty ultimately imposed by the court of the Labor Workforce Development Agency, and there is no discretion afforded within the statute for a lessened amount where facts suggest even the minimum penalty would be arbitrary or oppressive under the circumstances.

Evaluation of Classification Status:

Whether workers qualify as independent contractors can be a close call. Whether or not the parties believe they are creating an employer-employee relationship may have some bearing on the question, but is not determinative since this is a question of law based on objective tests. Courts generally consider the degree of independent control that the worker has over the job to be performed. But there are some specific questions that the Internal Revenue Service and the Division of Labor Standards Enforcement, the state's enforcement agency, will ask.

Employers may benefit from assistance of counsel in evaluating their independent contractor classifications or for guidance of the appropriate criteria.

Stand By Me...But Do I Need To Pay You To Do It? Employee On-Call and Standby Time May Be Compensable

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The line for when employees are on or off the clock has become increasingly blurred, as even non-exempt employees are now frequently provided with Blackberries and iPhones, keeping them in virtual contact with their companies at all times. If the employee must carry the device because they would be required to respond to requests for assistance and emergencies, they may also be entitled to pay for on-call or standby time, regardless if that employee was actually called in to work or not.

In California, an employer is obligated to pay the wages of an hourly employee for all time that the employee is under the "control" of the employer. Determining whether on-call or standby time qualifies as such controlled time requires analyzing the restrictions placed on the employee to determine the extent to which the employee may use the time for their own purposes.

Is it Controlled or Uncontrolled?

California uses a two-part test to determine the extent of control an employer exerts over an employee and whether that time is compensable. The first question simply asks whether the restrictions are primarily for the employer's benefit. The second asks whether the employee is so restricted as to be unable to attend to private pursuits. *Madera Police Officers Assn. v. City of Madera* (1984) 36 Cal. 3d 403.

The factors to consider in answering this second question focus on whether an employee is on "controlled standby" include: (1) the degree to which the restrictions affect the employee's geographical movements; (2) the frequency of calls; (3) how quickly the employee must respond to a call; (4) whether the on-call employee can easily trade his on-call responsibilities with another employee, and (5) the extent of personal activities engaged in during on-call time.

On the other hand, an employee who is on standby and required to remain at the employer's work site is considered to be working and the employee must be compensated, even if the employee does nothing but simply wait for something to happen.

Bottom line, simply being on-call is insufficient on its own for standby time to be compensable. As well, requiring the employee to respond to call backs is not so inherently intrusive that the control test is met. Rather, each circumstance must be measured by totality of the restrictions. When in doubt, ask: Do the restrictions substantially restrict the employee's personal time while on stand-by such that he or she is effectively unable to engage in private pursuits? If so, standby and on-call time may very well be compensable time.

Published Opinion Affirms Judgment in Favor of Church-Run School

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Published decision, *Henry v. Red Hill Evangelical Lutheran Church of Tustin* (CA 4/3, G044556, 12/9/11), affirmed a successful Motion for Summary Judgment in favor of our client in a wrongful termination action brought under both state and federal laws. Edmund G. Farrell, III, Michael D. McEvoy and Maria A. Starn defended the right of the client church-run school to terminate the employee pre-school teacher based on the "faith-based values" of the church. Ms. Starn primarily authored the appellate brief.

The fourth district held that: the plaintiff's claim for wrongful termination was barred as the defendant, a nonprofit religious corporation, did not qualify as an "employer" under FEHA; the defendant's religiously motivated employment decision was exempt under Title VII of the 1964 Civil Rights Act; and, her claim for wrongful termination in violation of public policy was barred by the ministerial exception.

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New Legislation on Pre-Employment Credit Reports

Beginning January 1, employers may request a credit report for applicants or employees only in limited circumstances. Added to the Labor Code as § 1024.5, exceptions for private-sector employers include,

- managerial positions (if qualifying under the executive exemption)
- a position for which the information contained in the report is required by law to be obtained
- a position which involves regular access to certain personal information of others (including social security numbers)
- a position that involves regular access to cash totalling $10,000 or more during the workday

Rules regarding notice to applicants for denial of employment based on information obtained in a credit report continue to apply. See Civil Code § 1785.20.5.

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