EMPLOYMENT FLASH

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INSIDE

NLRB Recess Appointments Unconstitutional

On June 26, 2014, the U.S. Supreme Court found President Obama's three recess appointments to the National Labor Relations Board (NLRB) unconstitutional. *NLRB v. Noel Canning*, __ U.S. __ (2014). The Court held that President Obama improperly used the U.S. Constitution's Recess Appointments Clause while the Senate was in a three day recess in January 2012 to appoint three of the five NLRB members, finding that three days was too short a recess. While the three individuals appointed have since been replaced by others who have been confirmed by the Senate, this decision has significant implications for the validity of NLRB decisions rendered during the term of the recess appointees.

SEC Brings First-Ever Employment Retaliation Claim

On June 16, 2014, the Securities and Exchange Commission (SEC) brought its first anti-retaliation enforcement action, charging a hedge fund advisory firm with engaging in prohibited principal transactions and then retaliating against the employee whistleblower who reported the activity to the SEC. The alleged retaliatory actions taken against the whistleblower included removing him from his head trader position, assigning him as a compliance assistant, requiring him to investigate the conduct he reported and removing his supervisory authority. The fund and its owner, also charged with causing improper principal transactions, agreed to pay approximately $2.2 million, including a $300,000 penalty, to settle the charges.

EEOC Challenges Employer Severance Agreements

The U.S. Equal Employment Opportunity Commission (EEOC) recently sued two employers based on the form of their severance agreements. In each case, the EEOC argued that the agreement improperly limited the rights of a former employee to participate in the EEOC complaint process. *EEOC v. CVS Pharmacy, Inc.*, Civ. A. No. 1:14-CV-863 (N.D. Ill.); *EEOC v. CollegeAmerica Denver, Inc.*, Civ. A. No. 14-cv-01232-LTB-MJW (D. Co).

CVS is based on allegations the employer unlawfully conditioned the receipt of severance benefits on an overly broad severance agreement, interfering with the rights of employees to file discrimination charges and communicate with the EEOC and other fair employment practice agencies. The EEOC takes specific issue with the agreement's cooperation provision (which required the employee to notify the employer in the event of an administrative investigation), non-disparagement provision (which prevented the employee from disparaging the employer),

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EEOC Challenges Employer Severance Agreements *(continued from page 1)*

non-disclosure of confidential information provision (which generally required the employee to maintain the confidentiality of all employer information), release of claims provision (which included a broad release of any claim for unlawful discrimination) and covenant not to sue provision (by which the employee agreed not to bring any proceeding against the employer and, if breached, to be liable for the employer's legal fees). Significantly, the EEOC contends that a single carve-out from the covenant not to sue provision allowing for participation in EEOC proceedings and cooperation was insufficient. In this respect, the covenant not to sue allowed the employee to participate in federal, state and local governmental anti-discrimination agency proceedings and to cooperate with such agencies or their investigations. However, the sufficiency of this carve-out is criticized by the EEOC as "a single qualifying sentence that is not repeated anywhere else."

Similarly, *CollegeAmerica* is based on allegations that the private college employer violated federal age discrimination law due to a severance agreement with a former campus director that interfered with the employee's rights to file discrimination charges and communicate with the EEOC. The EEOC takes specific issue with provisions in the agreement conditioning the receipt of severance pay on not disparaging the employer and not contacting any governmental agency for the purpose of bringing a claim against the employer. Here, the employer sued the employee and sought a return of the severance consideration after the employee filed age discrimination charges with the EEOC. The EEOC took up the case against the employer and examined its other form severance agreements containing what it alleged to be similarly unlawful provisions.

The *CVS* and *CollegeAmerica* litigations indicate that the EEOC will aggressively enforce its longstanding position that a severance agreement may not interfere with an employee's right to file a charge and cooperate with an EEOC investigation. While the outcomes of these cases are worth following, employers should take care to avoid agreements that conflict with these principles.

New York State Transportation Industry Fair Play Act Becomes Effective

The New York State Commercial Goods Transportation Industry Fair Play Act is now in effect. N.Y. Labor Law § 862. The act addresses misclassification of workers in the commercial goods transportation industry and creates a presumption that a driver for a commercial goods transportation contractor is an employee. A "commercial goods transportation contractor" is broadly defined as an entity that compensates a driver who possesses a state-issued driver's license, transports goods in New York and operates a commercial motor vehicle. This presumption is similar to the presumption of employee status for drivers in certain industries under New York's unemployment insurance law. N.Y. Labor Law § 511(1)(b)(1).

To rebut the presumption of employment and establish a driver as an independent contractor, the individual must be paid on a Form 1099 and meet one of two tests. The first is the ABC test, which many states use to determine worker classification. To meet the ABC test, the individual must be: (A) free from control and direction in performing the job, both under contract and in fact; (B) performing services outside the usual course of the business for which the service is performed; and (C) customarily engaged in an independently established trade, occupation, profession or business that is similar to the service they perform.

The second test requires the presumptive employer to rebut the presumption by establishing the work is done by a separate business entity. The Act sets forth 11 criteria, all of which must be met for a sole proprietor, partnership, firm, corporation, or other entity to qualify as a separate business entity. The entity must: (1) be free from direction or control over the means and manner of providing the service, receiving only direction as to the desired result of the work or as required by federal rule or regulation; (2) not be subject to cancellation or destruction when its work with the presumptive employer ends; (3) have invested substantial capital in its business entity beyond ordinary tools and equipment; (4) own or lease the capital goods, gain profits or bear losses; (5) make its services available to the general public or others in the business community on a continuing basis; (6) if required by law, provide services reported on a Form 1099; (7) perform services in its own name under a written contract with the presumptive employer, which identifies the relationship as that of independent contractors or separate business entities; (8) obtain and pay for any required license or permit in its own name or, if allowed by law, pay for the use of the presumptive employer's license or permit; (9) hire its own employees without the presumptive employer's approval and pay those employees without reimbursement from the presumptive employer; (10) not have its own employees represented to be employees of the presumptive employer; and (11) have the right to perform similar services for others on whatever basis and whenever it chooses.

The act imposes strict civil and criminal penalties. It establishes a civil penalty of up to a $2,500 fine per misclassified employee for a first willful violation and up to $5,000 per misclassified employee for a second willful violation within a five-year period. Violation of the act also may constitute a

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misdemeanor, and corporate officers, directors and certain shareholders who knowingly permit violations to occur may be personally liable for civil and criminal penalties. A conviction for a willful violation may preclude the commercial goods transportation contractor from bidding on public contracts for a one to five-year period. The act also requires that all commercial goods transportation employers post a notice, available on the Department of Labor's website.

California Upholds Mandatory Class Action Arbitration Waivers

On June 23, 2014, the California Supreme Court held that arbitration agreements with mandatory class action waivers generally are enforceable in light of the U.S. Supreme Court's ruling in *AT&T Mobility LLC v. Conception* but that the Federal Arbitration Act (FAA) does not preempt state law prohibiting waiver of representative actions under the Labor Code Private Attorneys General Act of 2004 (PAGA). *Iskanian v. CLS Transportation Los Angeles, LLC*, __ Cal. __, __ Cal Rptr. __ __ (2014) (forthcoming). The court found no conflict with the FAA's objective of promoting arbitration as a forum for private dispute resolution, noting that a Private Attorneys General Act (PAGA) representative action is a public enforcement action unlike the situation where the claim concerns two private parties agreeing to waive the right to assert claims in a class action. Therefore, the court allowed the individual damages claims to proceed to arbitration, but held that the PAGA claims should remain with the trial court.

The opinion leaves to remand several unanswered questions that will impact future litigation, including the appropriateness of bifurcating PAGA claims, which are not subject to mandatory arbitration or waiver, from the claims to be arbitrated individually, and whether, if bifurcation occurs, arbitration should be stayed under California Code of Civil Procedure 1281.1.

In related developments, the U.S. Court of Appeals for the Ninth Circuit recently decided two cases upholding arbitration agreements entered into with California employees. First, Bloomingdales successfully defended its arbitration agreement containing a class action waiver against a former sales associate who was prevented from pursuing a state law class action alleging unpaid overtime. *Johnmohammadi v. Bloomingdales, Inc.*, No. 12-55578 (9th Cir. June 23, 2014). The employee unsuccessfully argued that federal labor laws caused the class action waiver to be unenforceable. Second, Nordstrom successfully defended its arbitration agreement containing a class action waiver against an employee's claim that she was not provided with proper notice of the changes because the employer failed to explain that the changes would not go into effect for 30 days, consistent with company policy. *Davis v. Nordstrom, Inc.*, No. 12-17403 (9th Cir. June 23, 2014). The court held that although the employer's "communications with its employees were not the model of clarity," they met minimal California law notice requirements because employees received a letter notifying them of the changes, and they were not enforced during a 30-day notice period.

California PAGA Actions May Not be Removed to Federal Court on the Basis of CAFA

In *Baumann v. Chase Investment Services*, No. 12-55644, 2014 WL 983587 (9th Cir. Mar. 13, 2014), the Ninth Circuit held that the federal Class Action Fairness Act (CAFA) does not provide a basis for removing a representative action under California's PAGA from state to federal court. PAGA is a California law that allows aggrieved employees, acting as "private attorneys general," to sue their employers to collect civil penalties for certain Labor Code violations. In a PAGA action, 75 percent of the penalties recovered are returned to the state, and the remaining 25 percent is returned to the aggrieved employees.

CAFA permits a case to be heard in federal court if certain criteria are met — if the class size is at least 100, the amount at-issue is at least $5 million dollars, there is a diversity of citizenship between the plaintiffs and the defendants, and if the case is a class action under the Federal Rules of Civil Procedure (FRCP) or a similar rule authorizing class or representative actions. The Ninth Circuit contrasted PAGA actions with traditional class actions under FRCP 23, noting that PAGA actions do not have the same class certification requirements as FRCP 23 class actions, and that the two differ in other ways, such as in their preclusive effect and the nature of the remedy. Thus, CAFA will not provide an avenue for employers to remove a PAGA action to federal court.

The consequence of this case is that PAGA actions that are filed in California state court are more likely to remain in state court, a forum which is perceived as more employee-friendly when compared to federal court. However, PAGA actions are often accompanied by other civil claims styled as a "class action," and those combined actions may not be subject to the *Baumann* holding.

Supreme Court Upholds Michigan's Public Affirmative Action Ban

On April 22, 2014, the U.S. Supreme Court upheld a Michigan law banning affirmative action in public university admissions. *Schuette vs. Coalition to Defend Affirmative Action*, 134 S.Ct. 1623 (2014). The Michigan ballot initiative, Proposal 2, amended the Michigan state constitution to prohibit

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discrimination and preferential treatment based on race, sex, color, ethnicity or national origin in public employment, public education and public contracting. Proposal 2 passed in November 2006, and various interest groups challenged it as applied to public universities and preferential treatment based on race. The U.S. Court of Appeals for the Sixth Circuit, in a decision reversed by the Supreme Court, held that the law violated the Equal Protection clause of the 14th Amendment by making it more difficult for minorities to achieve legislation in their interest in the political process.

Schuette is a 6-2 decision, and the Court issued five separate opinions. Justices Roberts, Scalia and Breyer wrote concurring opinions, and Justice Sotomayor authored a dissent. Justice Kagan recused herself. The controlling opinion, written by Justice Kennedy, emphasized that this case presented a different question from the Supreme Court's prior public education affirmative action cases. While previous cases addressed the constitutionality of considering race in the admissions process, *Schuette* focused on the ability of a state's citizenry to reject affirmative action. Because the case involved voter-mandated race-neutrality, rather than intentional discrimination, the Court held that its affirmative action precedent and the Equal Protection clause were not at issue. The Court's holding validates affirmative action bans passed by Michigan and other states. While states without such bans may continue to use affirmative action programs in accordance with the Court's prior precedent, the divisions within the Court reflect that affirmative action in general remains an unsettled area of law.

Severance Payments As Wages Under FICA

In *United States vs. Quality Stores, Inc.*, the U.S. Supreme Court held that in most cases, severance payments constitute wages under the Federal Insurance Contributions Act (FICA) and are therefore subject to withholding. 134 S.Ct. 1395 (2014). The Supreme Court's decision in *Quality Stores* resolves a split created by the Sixth Circuit, as the U.S. Courts of Appeals for the Federal Circuit, Third Circuit and Eighth Circuit previously had held that severance payments constitute wages subject to FICA taxes. Employers generally are obligated to withhold and pay FICA tax on employee wages, which includes separate taxes for social security and Medicare. The Court started with the proposition that the definition of wages under FICA is broad, and includes "all remuneration for employment." The Court reasoned that severance payments are necessarily "for employment," as severance is not paid to non-employees. Furthermore, severance payments, like other employee benefits, are frequently tied to years of service and the employee's position, bolstering the position that the payments are "for employment." The Court also looked to FICA's specific exemptions from the definition of wages, which "reinforce[] the broad nature of FICA's definition of wages." 134 S.Ct. at 1400.

First Amendment Protection in Retaliation Suit

On June 19, 2014, the Supreme Court held that a public community college employee could claim First Amendment protection to proceed with a retaliation claim where his employment was allegedly terminated based on his testimony in criminal fraud actions against a state senator. In *Lane v. Franks*, 573 U.S. __(2014), an employee was terminated by the college's then-president after testifying against a former Alabama state senator in a criminal proceeding. The employee brought suit against the college and its president under 42 U.S.C. § 1983, which protects an individual›s right to sue state government actors, claiming that the college and its president violated the First Amendment by terminating his employment in retaliation for testifying.

The Supreme Court held that the employee could state a claim against the college but not against its president in his individual capacity. Appling the balancing test in *Pickering v. Board of E. of Township High School Dist. 206, Will Cty.*, 391 U.S. 563, 568 (1968), the Court held that the employee's interest as a citizen in commenting on matters of public concern outweighed the state's interest as an employer in promoting the efficiency of public services. The Court found the college did not assert an adequate government justification on which to base the termination; for example, that the employee's testimony was false or erroneous or that it concerned sensitive, confidential or privileged information. With respect to the claim against the college president, the Court reasoned that, given the lack of definitive precedent, the president reasonably believed a government employer could terminate an employee because of testimony given under oath but outside the scope of ordinary job responsibilities.

NLRB Regional Director Finds College Football Players Are Employees

On March 26, 2014, Region 13 of the NLRB issued a decision holding that Northwestern University football players receiving grant-in-aid scholarships who have not exhausted their playing eligibility are employees eligible to unionize under the National Labor Relations Act (NLRA). *Northwestern University, Case No. 13-RC-121359.* Further, the region directed that an immediate secret ballot election be held by the eligible players to determine whether they should be represented by the College Athletes Players Association, the union that sought to represent them. As predicted, on April 9, 2014, Northwestern requested that the full NLRB to review and overturn this decision. The NLRB granted Northwestern's request for review on April

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24. Parties and amici have been invited to file briefs by June 26, 2014, and the parties may file responsive briefs by July 10, 2014. In the interim, the region conducted an election on April 25, 2014, the results of which will be impounded until the NLRB review is complete.

More specifically, the regional director's decision held that "players receiving scholarships to perform football-related services for [Northwestern] under a contract for hire in return for compensation are subject to [Northwestern's] control and are therefore employees within the meaning of the [NLRA]." The regional director also found that the NLRB's 2004 *Brown University* decision, holding that graduate students were not employees, was not applicable and, even if applicable, was distinguishable. Unlike the graduate students in *Brown University*, the regional director concluded that players are not "primarily students," their athletic duties are not a core element of their degree requirements, they are supervised by football coaches not academic faculty members and their compensation is unlike traditional financial aid.

The regional director's decision is significant because of its liberal construction of NLRA protections and is being closely watched by, among others, universities, players and the sports industry as it makes its way through the NLRB.

New York City's Earned Sick Time Act Goes Into Effect

On April 1, 2014, New York City's Earned Sick Time Act became effective. The law generally requires that New York City employers provide either paid or unpaid sick time to their employees, depending on factors such as the number of employees. Employees who work in New York City are covered regardless of where they reside or whether they work part time or full time.

Employers must provide paid sick leave if they have five or more employees who are each hired to work more than 80 hours per calendar year. Employers must provide unpaid sick leave if they have fewer than five employees who are each hired to work more than 80 hours per calendar year. Leave is accrued at the rate of one hour for every 30 hours worked, up to a maximum of 40 hours of sick leave per calendar year, with the exception of certain employees, including those covered by a currently effective collective bargaining agreement.

Employers employing one or more domestic workers who have been employed for at least one year and who work more than 80 hours per calendar year must provide paid sick leave of two days per calendar year.

Employees may begin to use sick leave on the later of (1) July 30, 2014, or (2) 120 days after employment begins. Sick leave may be used for the care and treatment of the employee or the employee's family member. Under the act, family members include an employee's child, spouse, domestic partner, parent, sibling, grandchild or grandparent, or the child or parent of an employee's spouse or domestic partner. The Earned Sick Time Act contains provisions prohibiting retaliation; requiring recordkeeping for a period of three years; and addressing notice, documentation of leave and annual carryover of sick leave. All employees must receive a Notice of Employee Rights, available on the New York City government's website, on their first day of employment, and existing employees should have received such notice no later than May 1, 2014.

Employment Flash **provides information on recent developments in the law affecting the corporate workspace and employees. If you have any questions regarding the matters discussed in this newsletter, please call one of the following attorneys or your regular Skadden, Arps contact:**

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