Employment Flash

Skadden

April 2018

In This Issue:

Four Times Square
New York, NY 10036
212.735.3000

US Supreme Court Narrows Definition of Whistleblower

In *Digital Realty Trust, Inc. v. Somers*, 138 S. Ct. 767 (2018), the U.S. Supreme Court declined to expand the term "whistleblower" under the Dodd-Frank Act to include employees who report potential violations of securities laws internally within their organizations rather than externally to the Securities and Exchange Commission (SEC). In its unanimous decision, the Supreme Court showed deference to the statutory language that defines "whistleblower" as those who provide "information relating to a violation of the securities laws to the [SEC]." The ruling reversed the U.S. Court of Appeals for the Ninth Circuit's decision to extend anti-retaliation whistleblower protections to an employee who had complained internally about an alleged violation of the Sarbanes-Oxley Act. The ruling could result in fewer individuals being entitled to whistleblower incentives and anti-retaliation protections. In addition, the ruling may encourage employees to report alleged violations directly to the SEC before employers can take corrective action.

US Supreme Court Rules Auto Service Advisers Are Exempt From Overtime Pay

On April 2, 2018, the U.S. Supreme Court ruled in *Encino Motorcars, LLC v. Navarro et al.*, No. 16-1362, 584 U.S. ____ (2018), that auto service advisers are exempt from the overtime pay provisions of the Fair Labor Standards Act (FLSA). In a 5-4 decision, the Court ruled that service adviser employees — employees at car dealerships who advise customers about repair work — fall under an FLSA exemption from overtime pay that is applicable to "any salesman, partsman or mechanic primarily engaged in selling or servicing automobiles." The Supreme Court's ruling overturned a Ninth Circuit decision and rejected long-standing precedent that FLSA exemptions are to be narrowly construed against employers.

The case began in 2012 when service advisers at a California auto dealership filed suit against their employer for allegedly violating the FLSA by paying them only commissions, even if they worked longer than the standard 40-hour work week. The service advisers claimed they did not actually "sell" or "service" cars and therefore did not fall under the FLSA exemption. The Supreme Court held that the best reading of the statute is that service advisers are exempt because they are "salesmen" who "sell customers services for their vehicles." The Court gave a new "fair reading" directive to lower courts when they interpret the FLSA — a directive that deviates from the long-standing principle of "narrow construction." The Court explained that because the FLSA provides no "textual indication" that its exemptions should be construed narrowly, there is no reason to give the exemptions "anything other than a fair (rather than a 'narrow') interpretation." This "fair reading" rule could impact the interpretation and application of other FLSA exemptions.

DOJ Agrees to Settle Prosecution of Employee No-Poach Arrangements

The Department of Justice (DOJ) announced on April 3, 2018, that it had agreed to settle a civil antitrust lawsuit against two companies that had entered into an employee "no-poach" agreement. According to the DOJ, the two companies reached an agreement in 2009 not to solicit, recruit, hire without prior approval or otherwise compete with each other for employees. In its lawsuit, the DOJ argued that typically the two companies compete with one another to attract, hire and retain skilled employees. It stated that the no-poach agreement violated antitrust laws because it restricted competition for workers in the industry by limiting access to better job opportunities, hindering job mobility and depriving workers of competitively significant information that could have been used to negotiate better terms and conditions of employment.

As part of the settlement agreement, the two companies are prohibited from entering into, maintaining or enforcing employee no-poach agreements or no-poach provisions with other companies, subject to a limited number of exceptions, such as employee nonsolicitation agreements entered into ancillary to legitimate business collaborations. In addition, the two companies agreed to notification and compliance measures that prevent the companies from entering into these types of agreements in the future. They also agreed to provisions that enhance the enforceability of the consent decree, including one lowering the standard of proof for alleged violations of the consent decree and a cost-shifting provision requiring the companies to reimburse taxpayers for investigation and enforcement costs. The DOJ has indicated that it will pursue these new provisions in future consent decrees.

This lawsuit marked the first "no-poach" prosecution since the DOJ and the Federal Trade Commission issued its "Antitrust Guidance for Human Resource Professionals" in October 2016. In that guidance and elsewhere, the DOJ stated that it would pursue criminal, felony charges against culpable companies and individuals entering into employee no-poach arrangements. In its April 2018 lawsuit, however, the DOJ pursued a civil action because the companies formed and terminated the employee no-poach agreement prior to the issuance of the October 2016 antitrust guidance. Thus, the possibility of criminal action remains for companies that enter into or continue to honor employee no-poach agreements after October 2016.

Approximately one week after the DOJ announced the proposed settlement, an employee filed a putative class action against the two companies for the same alleged violations of antitrust laws and is seeking compensatory damages, treble damages and a permanent injunction, among other relief.

New York Enacts Anti-Sexual Harassment Legislation

On April 12, 2018, New York Gov. Andrew M. Cuomo signed into law comprehensive anti-sexual harassment legislation. As noted below, many sections of the new law will not go into effect until at least July 11, 2018. Among other things, the new law prohibits mandatory arbitration of sexual harassment complaints. This section of the law applies to current and future contractual clauses mandating arbitration of sexual harassment claims and takes effect on July 11, 2018. Moreover, where there is a settlement of lawsuits involving sexual harassment allegations, the new law prohibits the use of nondisclosure agreements (NDAs) and requires court approval of such settlements. In particular, this section of the law pertaining to NDAs, which becomes effective on July 11, 2018, adds Section 5-336 to the General Obligations Law (GOL) and Section 5003-b to the Civil Practice Law and Rules (CPLR). Under GOL Section 5-336, employers are prohibited from including an NDA in any settlement of a sexual harassment claim unless the complainant requests confidentiality. If he or she does so, the terms must first be provided to all parties. The complainant then has 21 days to consider the terms, and, after 21 days, if the term is still the complainant's preference, the term must be memorialized in an agreement signed by all parties. The complainant then has seven days to revoke the agreement, which shall not be effective or enforceable until the revocation period expires. GOL Section 5-336 appears to apply to settlements of all claims of sexual harassment, not just those filed in court. CPLR Section 5003-b includes the same provisions as GOL Section 5-336 but appears to apply to settlements of sexual harassment lawsuits.

In addition, the law requires every employer to adopt a robust sexual harassment prevention policy that provides the same or greater protections as those found in the model policy established by the New York State Division of Human Rights and provide annual anti-sexual harassment training to employees. This section of the law takes effect on October 9, 2018.

Furthermore, firms competing for work from the state or any public department or agency of the state must submit a certification, under penalty of perjury, that they have implemented a written sexual harassment policy and provide annual sexual harassment training to all employees. The section takes effect on January 1, 2019.

The new law also extends protections to contractors, vendors, consultants and other nonemployees, who are not covered by existing New York state laws prohibiting sexual harassment. Accordingly, the new law makes employers liable to nonemployees when employers should have known that the nonemployees were subjected to workplace sexual harassment and the employers failed to take immediate and appropriate corrective action. This part of the law takes effect immediately and applies to all employers in the state.

New York Creates New Employer Compensation Expense Program

On April 12, 2018, Gov. Cuomo signed into law the New York Legislature's 2018-19 budget bill, which addressed several provisions of the federal Tax Cuts and Jobs Act. In particular, the bill implemented a new "Employer Compensation Expense Program," effective as of January 1, 2019. The program will allow New York employers to opt in to pay a new payroll tax that subjects employers to a 5 percent tax on all annual payroll expenses in excess of $40,000 per employee. Each such employee will then receive a corresponding tax credit on his or her wages, offsetting personal income tax in an amount equal to the payroll tax. Thus, employers can incur a payroll tax expense that could be deductible at the federal level and also potentially reduce certain employees' state tax liability.

The program will be phased in over three years, beginning January 1, 2019, at 1.5 percent and increasing to 3 percent in 2020 and ultimately to 5 percent by January 1, 2021. As mentioned in our April 9, 2018, client alert "New York State Responds to Federal Tax Reform," there are a number of factors that should be evaluated by any taxpayer considering whether to make this election, including whether the Internal Revenue Service will challenge the validity of employer deductions.

Salary History Ruling Regarding Gender Pay Inequities

On April 9, 2018, the Ninth Circuit held that an employee's salary history cannot be used to justify disparate pay between men and women under the Equal Pay Act (29 U.S.C. §206(d)) (EPA). The court's decision in *Rizo v. Yovino*, No. 16-15372, 2018 WL 1702982 (9th Cir. Apr. 9, 2018) overturned its 1982 ruling in *Kouba v. Allstate Insurance Co*., 691 F.2d 873, which held that employers could use prior salary to determine employees' wages without violating the EPA.

The EPA requires that women and men be paid the same wages for the same or substantially similar work. The EPA offers four statutory exceptions that allow employers to provide disparate pay to women and men: (i) a seniority system, (ii) a merit system, (iii) a system that measures earnings by quantity or quality of production, and (iv) a differential based on any other factor other than sex. These exceptions operate as affirmative defenses. The Ninth Circuit in *Rizo* held "that 'any other factor other than sex' is limited to legitimate, job-related factors such as a prospective employee's experience, educational background, ability, or prior job performance." The Ninth Circuit held that salary history does not fall within an exception to the EPA, but the court did "not attempt to resolve its applications under all circumstances." The court stated that it reserved for subsequent cases the questions of "whether or under what circumstances, past salary may play a role in the course of an individualized salary negotiation."

The Ninth Circuit ruling in *Rizo* is directly at odds with a U.S. Court of Appeals for the Seventh Circuit ruling in *Wernsing v. Ill. Dept. of Human Services*, 427 F.3d 466 (2005) that salary history is considered a "factor other than sex" under the EPA. U.S. Court of Appeals for the Eighth Circuit precedent aligns closely with the Seventh Circuit's interpretation of this EPA exception. The U.S. Courts of Appeals for the Second, Sixth, Tenth and Eleventh Circuits have adopted an interpretation of this EPA exception that is similar to the Ninth Circuit's interpretation, but these circuits have not gone so far as to prohibit the consideration of salary history altogether.

The Ninth Circuit's decision affects employers in Alaska, Arizona, California, Hawaii, Idaho, Montana, Nevada, Oregon and Washington. In addition, several states and localities have recently passed legislation prohibiting employers from inquiring into applicants' salary history during the hiring process. They include, but are not limited to, California, Delaware, Massachusetts, New York City, Albany County (New York), Oregon and Puerto Rico.

DOL to Test Voluntary Reporting for Wage Violators

In March 2018, the Department of Labor (DOL) announced a six-month pilot program allowing employers to self-audit and self-report violations of the FLSA's overtime and minimum wage provisions. The program, titled the Payroll Audit Independent Determination (PAID), will be implemented by the DOL's Wage and Hour Division (WHD). PAID was designed to provide a way for employers to avoid litigation and ensure that employees timely receive any back pay they are owed. PAID requires an affected employee who accepts an employer's payment of back pay to sign a narrowly tailored release of claims for the specific violations and time period identified by the employer.

PAID offers various benefits to employers, including the avoidance of costly litigation and payment of liquidated damages, civil penalties and legal fees under the FLSA. However, such benefits are limited to certain circumstances. For example, employers currently under investigation or litigating wage and hour claims cannot take advantage of PAID to resolve those particular matters. The potential for new litigation also remains because affected employees have a choice between accepting back pay and executing a release of claims or, instead, pursuing litigation. In short, employees are not required to rely on employers' good faith reporting of violations and can file suit.

Additionally, PAID raises some questions and issues, namely whether self-reporting will expose employers to greater scrutiny from the WHD, whether affected employees who refuse to accept payment will be permitted to use an employer's voluntary report to the WHD as evidence in the litigation of the claims and whether the release of claims will be limited to the FLSA. Following the six-month test period, the DOL may resolve some of these issues — and any other issues discovered during that period — before implementing a permanent program or, depending on the success of PAID, decide to discontinue the program.

NLRB Reverts Back to BFI Joint Employer Test

On February 26, 2018, the National Labor Relations Board (NLRB) vacated its recent December 14, 2017, decision in *Hy-Brand Industrial Contractors, Ltd. and Brandt Construction Co*., 365 NLRB No. 156 (2017), which overturned the landmark joint employer test described in *Browning-Ferris Industries*, 362 NLRB No. 186 (2015) (the BFI Test). Thus, the BFI Test remains in effect. Under the BFI Test, a company and its contractors or franchisees can be deemed to be a single joint employer under the National Labor Relations Act (NLRA), even if an entity has not exercised overt control over workers' terms and conditions of employment. Instead, all that is necessary to show joint employer status is "indirect control" or the ability to exert such control over workers' terms and conditions of employment. The BFI Test has important implications for franchisors and franchisee employees. The NLRB's decision to vacate the *Hy-Brand* decision resulted from an internal agency report issued by NLRB Inspector General David P. Berry finding a potential conflict of interest in NRLB member Bill Emanuel's participation in the case. An appeal of *Browning-Ferris* is currently pending before the U.S. Court of Appeals for the District of Columbia Circuit, but at least for now, the BFI Test is once again the controlling test for joint-employer determinations.

Second Circuit Rules Sexual Orientation Is a Protected Class Under Title VII

On February 26, 2018, in *Zarda v. Altitude Express*, 883 F.3d 100 (2d Cir. 2018), the Second Circuit ruled that discrimination on the basis of sexual orientation qualifies as sex discrimination and is prohibited under Title VII of the Civil Rights Act. The case arose when the former employee alleged that his employment was terminated in violation of Title VII when he told a client about his sexual orientation. The Second Circuit explained that, because one cannot fully define a person's sexual orientation without identifying his or her sex, sexual orientation is a function of sex, and because sex is a protected category under Title VII, sexual orientation is also a protected category. The Second Circuit rejected the argument that one could discriminate against an employee because he is gay and not because he is a man. It explained that an employer's failure to reference gender directly does not change the fact that an employee who is gay is simply a man who is attracted to men and that, had such employee been a woman attracted to men, the discrimination would not have arisen — therefore presenting a case of "but for" discrimination based on sex. The Second Circuit explained that the reach of Title VII has expanded since its passage and the court's decision is consistent with that expansion.

NLRB Memoranda Developments

In February 2018, the NLRB's Division of Advice released 44 memoranda related to the interpretation of the NLRA and dating back to 2009. Two are from 2018. In a January 12, 2018, memorandum, the Division of Advice found that an employer did not violate Section 8(a)(1) of the NLRA when it discharged an employee without informing the employee of the reason for the termination. The memo applied the NLRB's decision in *Continental Group*, 357 NLRB 409, 412 (2011), which held that activity that may not otherwise be protected under Section 7 is protected when it "touches the concerns animating Section 7." The former employee argued that his employment was terminated because he discussed the conditions of his employment transfer in violation of the employer's unlawfully broad confidentiality rule. The memorandum concludes that, under the *Continental Group* test, discipline for such activity only violates the NLRA when the employer directly or indirectly informs the employee that the reason for the discipline is violation of the unlawful rule. Because the employer did not reference the confidentiality rule in connection with the termination, the Division of Advice concluded that the employer's conduct was permissible. The memo nonetheless expressed doubts about the legality of the confidentiality rules, which instructed employees to keep internal communications confidential.

In another memorandum dated January 16, 2018, the Division of Advice concluded that an employer did not violate Section 8(a)(1) of the NLRA when it discharged an employee who wrote and circulated a memorandum critiquing its diversity initiatives. The former employee claimed that its former employer violated the NLRA when it terminated his employment because his speech was protected. The memorandum that the former employee circulated "argued that there were immutable biological differences between men and women that were likely responsible for the gender gap in the tech industry at large and the Employer in particular." The Division of Advice concluded that "while much of the Charging Party's memorandum was likely protected, the statements regarding biological differences between the sexes were so harmful, discriminatory, and disruptive as to be unprotected." The Division of Advice recommended that the regional director dismiss the charge because it determined that the employer discharged the employee because of his unprotected discriminatory statements.

Delivery Driver Classified as Independent Contractor

On February 8, 2018, the U.S. District Court for the *Northern District of California in Lawson v. Grubhub, Inc.*, 2018 WL 776354 (N.D.Cal., 2018), concluded that a driver for a food delivery service was properly classified as an independent contractor. In California, worker classification cases have been reviewed under the Borello test, which focuses on an entity's control over the worker in question and, in addition, reviews how the worker is supervised, who provides the worker's equipment and the degree of skill involved. Applying the Borello test, the court held that a determinative factor was that the company exercised a minimal amount of control over the driver's work; the driver could control his work schedule by, among other things, deciding the specific days and number of hours per day that he would work. However, the court noted that some factors weighed in favor of his classification as an employee, including the company's ability to terminate the driver's services at will with 14 days' notice, the lack of special skills required for the job and the fact that the driver's work was part of the company's regular business.

More recently, on April 30, 2018, the California Supreme Court released its decision in *Dynamex Operations West, Inc. v. Superior Court*, Opinion No. S222732, addressing the legal standard for determining whether a worker is an employee or an independent contractor for purposes of wage and hour laws. The court eschewed the Borello test and concluded that "in determining whether, under the suffer or permit to work definition, a worker is properly considered the type of independent contractor to whom the wage order does not apply, it is appropriate to look to a standard, commonly referred to as the 'ABC' test. ... Under this test, a worker is properly considered an independent contractor to whom a wage order does not apply only if the hiring entity establishes: (A) that the worker is free from the control and direction of the hirer in connection with the performance of the work, both under the contract for the performance of such work and in fact; (B) that the worker performs work that is outside the usual course of the hiring entity's business; and (C) that the worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed for the hiring entity."

International Spotlight

The European Union's General Data Protection Regulation

The General Data Protection Regulation (GDPR), effective as of May 25, 2018, will regulate the processing of personal data across the European Union. The GDPR aims to enhance and harmonize current EU rules related to the transfer of personal data across the EU. The GDPR focuses on processing personal data in the customer and commercial contexts, but it will also have a material impact on employers that process the personal data of prospective, current and former employees, independent contractors and other workers.

The key principles of current EU data protection legislation will remain unchanged by the GDPR, but the GDPR implements several changes that will significantly impact employers. Specifically, it:

- expands the categories of data that are classified as "sensitive" to include data relating to racial or ethnic origins; political opinions; religious or philosophical beliefs; trade union membership; genetic or biometric data processed for the purpose of uniquely identifying a person; health information; and data relating to sex life and sexual orientation. Sensitive personal data is subject to stringent processing rules;
- imposes additional obligations on a "data processor," which is any person who processes personal data on behalf of another person. The GDPR requires data processors to:
  - obtain the consent of the "data controller" — the person who determines the purposes for which and the manner in which any personal data are, or are to be, processed — before subcontracting out any data processing;
  - maintain a record of their data processing activity;
  - ensure that appropriate technical and security measures are in place when managing personal data; and
  - notify the data controller of any data breach.

Employers must update contractual terms between employers and entities that process personal data on their behalf, such as payroll or reference check service providers, to ensure that these obligations are incorporated into the relevant contracts;

- increases data controllers' accountability to regulators regarding their respective data processing activities. For example, data controllers and data processors are required to maintain detailed records of their respective processing activities. The GDPR requires data controllers to notify the relevant regulator within 72 hours of discovering a personal data breach that could result in a data privacy risk to data subjects, if feasible. Accordingly, employers must establish and maintain clear policies and procedures to enable staff to report data breaches in an efficient and effective manner;
- has extraterritorial application. The GDPR applies to data controllers and data processors established in the EU, as well as to data controllers and data processors that offer goods or services to EU residents and that monitor the behavior of EU residents in the EU;
- imposes a maximum fine for breach of the regulations of the greater of 4 percent of the organization's worldwide turnover or €20 million. The maximum penalty under existing U.K. data protection legislation is £500,000; and
- requires that a data subject's consent to process his or her personal data be explicit, informed and freely given. Because this is a high threshold to meet, employers are advised to rely on having a legitimate business purpose to process data.

The GDPR will result in an enhanced level of regulation of personal data within the EU and with respect to multinational businesses with operations in the EU. In the transactional context, employers must conduct the proper risk assessments and establish and maintain adequate contractual protections, policies and procedures before sharing any employee personal data with acquirers and investors, and before transferring personal data outside the European Economic Area to countries such as the United States. Organizations that currently rely on standard contractual clauses (or model clause agreements) should review and revise those clauses and agreements as necessary when new GDPR compliant standard contractual clauses are published by the European Commission.

Contacts in the Labor and Employment Law Group

Karen L. Corman
Partner / Los Angeles
213.687.5208
karen.l.corman@skadden.com

David E. Schwartz
Partner / New York
212.735.2473
david.schwartz@skadden.com

Helena J. Derbyshire
Of Counsel / London
44.20.7519.7086
helena.derbyshire@skadden.com

Stéphanie Stein
Of Counsel / Paris
33.1.55.27.11.56
stephanie.stein@skadden.com

Risa M. Salins
Counsel / New York
212.735.3646
risa.salins@skadden.com

Ulrich Ziegler
Counsel / Frankfurt
49.69.74220.150
ulrich.ziegler@skadden.com

Anne E. Villanueva
Associate / Palo Alto
650.470.4596
anne.villanueva@skadden.com