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DLSE Permits Salary Reductions in Response to Economic Downturn

As a general rule, exempt employees must be paid their full salaries for workweeks in which they perform any work. There are exceptions, such as when an employee misses a day or more for personal reasons (other than sickness or disability) or when the employee starts employment mid-week. But an employer that makes improper reductions in exempt employees' salaries risks losing the exemption and exposes itself to claims for years' worth of unpaid overtime.

What about when the employer reduces the schedule and salaries of exempt employees as a way to control costs? In an Opinion Letter from August 19, 2009, California's Division of Labor Standards Enforcement (DLSE) concluded that the law permits such actions in appropriate circumstances.

The DLSE opinion responded to the following fact pattern. An employer struggling due to the present economic downturn wants to reduce from five scheduled workdays per week to four. The impact on hourly employees is obvious. They would not be paid for the time they don't work. As for exempt employees, the employer would reduce their salaries by 20 percent. The employer intends this to be a temporary change and will return to a five-day week and full salaries as soon as business conditions improve.

Contradicting an Opinion Letter it issued in 2002, the DLSE said the change is permissible, provided that it (1) is not intended to circumvent the rule that employees be paid their full salaries in any week they perform work and (2) does not reduce their compensation below the minimums required under applicable law. The DLSE emphasized that these steps would only be available to employers that "experienced significant economic difficulties due to the present severe economic downturn." It further emphasized that this was a one-time, temporary adjustment. But in those circumstances, the DLSE granted employers a degree of flexibility to reduce exempt employees' work schedules and salaries without jeopardizing their exempt status.

Employers wishing to explore this option can contact any of our California employment lawyers. By then, the DLSE may have changed its position on this subject yet again. ◆

Restaurant Fined for Firing Worker Who Was Breastfeeding Baby During Breaks

In a decision issued by the California Fair Employment and Housing Commission, a Los Angeles taco shop was ordered to pay $46,000 to a female employee who was fired for breast feeding her baby in a car during breaks. The written opinion states: "Ms. Chaves suffered an egregious violation of her civil rights that is not tolerated in California." *DFEH v. Acosta Tacos* (DFEH Case No. E200708T-0097-00se). Employers must know that the California Labor Code requires employers to reasonably accommodate employees in their desire to "express breast milk at work" by providing breaks and a private "lactation area." The Labor Commissioner can assess a civil penalty of $100 per violation. ◆

California's New Aerosol Transmissible Disease Regulations Seek To Prevent Diseases in High-Risk Workplaces

California's Occupational Safety and Health Standards Board recently adopted regulations on aerosol transmissible diseases (ATDs) to address workplace exposure to airborne diseases in particular settings. The new regulations seek to ensure the health and safety of workers who are at increased risk of exposure to aerosol transmissible diseases such as TB, SARS, Avian flu and human influenza viruses (such as H1N1). While there are several levels of requirements for different types of facilities, most covered facilities must create an exposure control plan; implement practice controls; provide personal protective equipment, medical services and annual training to employees; and conduct appropriate recordkeeping. All employers covered by the regulations must provide all the required safeguards at no cost to the employees and during working hours. Employers are encouraged to review the new regulations and discuss compliance issues with counsel. The regulations can be found at Title 8, Section 5199 of the California Code of Regulations. ◆

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Warning to Management: You May Be Individually Liable Under the FLSA

Individual owners and managers of companies are not always protected from liability in wage and hour claims. In a recent case before the U.S. Court of Appeals for the Ninth Circuit, *Boucher v. Shaw*, a plaintiff sued three managers of his former employer, the Castaways Hotel, Casino and Bowling Center, for unpaid wages under the Fair Labor Standards Act (FLSA), among other claims. The defendants were the chairman and chief executive officer with a 70 percent ownership interest in the Castaways; the manager responsible for handling all labor and employment matters who had a 30 percent ownership interest; and the chief financial officer.

Although corporate agents and employees cannot be held individually liable for violations of California wage and hour laws, federal law provides a different avenue for redress. Such individuals may be liable under the FLSA if they exercise significant control over the company's operations. To make this determination, courts consider whether the managers have the power to hire and fire employees, the power to determine salaries, the responsibility to maintain employment records and other signs of operational control over significant aspects of the corporation's day-to-day functions. In this case, the court determined that each of the defendants exercised sufficient control over the Castaways to be individually liable for any violation of the FLSA.

The defendants did not contest liability under the FLSA and instead argued that they could not be liable for unpaid wages because the Castaways entered Chapter 7 liquidation and ceased operations after the plaintiff's paycheck for the unpaid wages was due to be issued. The court disagreed, holding that the company's bankruptcy—whether under Chapter 7 or Chapter 11—does not affect the liability of its individual managers under the FLSA. However, the court noted that if the liability of the managers *were* to affect the property of the company in bankruptcy, such as by a requirement that the company indemnify the managers, it may be necessary for the plaintiff to proceed against the managers through bankruptcy proceedings.

Cases like *Boucher* provide a cautionary tale in these economic times. While not frequently cited, federal standards do apply to most California employers and provide plaintiffs with an alternative source of compensation. Employers should expect to see a rise in claims against individual owners who have the ability to pay the debts of their business. Consequently, owners and managers should be cautioned and should not assume that filing for bankruptcy removes their potential individual liability under federal law. ◆

Good News….

- **Employers Not Liable for Acts of Foreign Suppliers**

The Ninth Circuit Court of Appeals has held that a U.S. company is not liable for the labor practices of foreign companies with which it does business. In *Doe v. Wal-Mart*, Case No. 08-55706, the plaintiffs alleged that: (1) they were "third-party beneficiaries" of Wal-Mart's supply contracts requiring certain labor standards, and (2) Wal-Mart was a joint employer of the workers of suppliers in China, Bangladesh and Indonesia. The federal appeals court rejected the plaintiffs' claims, saying that the company did not exercise an "immediate level of day-to-day" control and direction of the foreign employees.

- **Unions Cannot Bring Suit Over Meal Periods**

The California Supreme Court has ruled that a union does not have standing to sue over meal periods and rest breaks on behalf of its members. The Amalgamated Transit Union and the Teamsters sued three transportation companies under the California Labor Code and the Unfair Competition Law. The court held the unions did not suffer any requisite damage under either statute, and that the employees' rights under those statutes were not assignable. The case is *ATU v. Superior Court*, Cal. Supreme Court No. 151615.

- **Employers Can Avoid Class Action by Settling With Potential Plaintiffs**

After a wage and hour class action has been filed but before certification of the class, the employer is free to enter into settlement agreements with potential class members, a California Court of Appeal has ruled. *Chindarah v. Pick Up Stix* (2009) 171 Cal.App.4th 796, pet. for rev. denied, ___ Cal. ___ (2009). Notwithstanding Labor Code Section 206.5, which purports to prohibit the release of wage claims, the court found that a settlement and release is valid if there is a "bona fide dispute" over whether any wages are owed. The timing and execution of such a maneuver must be carefully planned, but this is a potential method for nipping a class action in the bud.

- **Ninth Circuit Denies Class Status for Home Loan Consultants**

In two separate opinions, federal appeals panels have denied wage and hour class status to mortgage consultants. In *Vinole v. Countrywide* (Case No. 08-55223) and *In Re Wells Fargo Home Mortgage Overtime Pay Litigation* (Case No. 08-15355-06-1770), the Ninth Circuit ruled that the district judges erred in finding that just because the companies uniformly classified these groups of employees as exempt, common issues would predominate over individual issues. The appeals court correctly exposed this logic as circular and fallacious. In the *Countrywide* case, the court wrote: "a district court abuses its discretion in relying on an internal uniform exemption policy to the near exclusion of other factors relevant to the predominance inquiry."

- **Summary Judgment for Employer on Claims of No "Interactive Process" and "Constructive Discharge"**

Failure to engage in an "interactive process" with a disabled employee to find some reasonable accommodation is a separate cause of action in California. Exactly what constitutes a sufficient "interactive process" is not entirely clear. One Court of Appeal has held that the employer was properly granted summary judgment on an employee's claim of failure to engage in an interactive process even though a reasonable jury could have found that the employer failed to continue the interactive process after an initial accommodation offer, where the employee suffered no injury inasmuch as no available accommodation was identified in discovery. The court also ruled that a change in employment status from full time did not amount to a constructive discharge. *Scotch v. Art Institute of California* (2009) 173 Cal.App.4th 986. ◆

No Inevitable Disclosure of Trade Secrets in California

All states (with the exception of New Jersey, New York, Texas and Massachusetts) have adopted some variation of the Uniform and Trade Secrets Act (UTSA) created in 1979 by the National Conference of Commissioners on Uniform State Laws. Despite almost nationwide adoption of the UTSA, state laws vary in how they define a "trade secret," how a trade secret violation is proven and the type of remedies available to a trade secret holder.

Increasingly utilized in nondisclosure agreements is an "inevitable disclosure" provision. The theory of "inevitable disclosure" allows an employer to seek an injunction to prohibit former employees from working for a competitor because the former employees will necessarily rely upon knowledge of the former employer's trade secrets in performing their new job duties. The doctrine of inevitable disclosure is typically used as an alternative to proving actual or threatened trade secret misappropriation. While this doctrine is relatively new and untested, it has been rejected in California. Under California law, an employer must produce evidence of an actual or threatened misappropriation in order to obtain an injunction against a former employee. The employee's mere knowledge of a trade secret and his or her change of employment will not suffice.

In *Les Concierges, Inc. v. Robeson*, 2009 WL 1138561 (N.D. Cal. Apr. 26, 2009), a California-based concierge service provider sought to enjoin a former employee from submitting proposals and soliciting business from Les Concierges' customers and prospective customers. Les Concierges argued that the former employee immediately began working for a direct competitor and appeared to be performing for his new employer the same or similar job duties he performed while employed by Les Concierges. The court determined that California does not recognize the inevitable disclosure doctrine and refused to grant an injunction merely because of the "employee's knowledge of trade secrets and subsequent change of employers."

At least two other California federal district courts and one California Court of Appeals have also rejected the inevitable disclosure doctrine. Those courts have found that the doctrine is directly contrary to California's public policy prohibiting an employer from entering into a noncompetition agreement with its employees. These courts found that the inevitable disclosure doctrine would create an "after-the-fact covenant not to compete" restricting employee mobility. See e.g., *Schlage Lock Co. v. Whyte*, 101 Cal.App.4th 1443 (2002); *Globespan Inc. v. O'Neill,* 151 F.Supp.2d 1229 (C.D. Cal. 2001); *Bayer Corp. v. Roche Molecular Sys. Inc.*, 72 F.Supp.2d 1111 (N.D. Cal. 1999).

In comparison, other states have utilized the inevitable disclosure doctrine to prevent employees from working for competitors. For example, a Texas court, applying Pennsylvania law, granted an injunction without any evidence that the former employee had actually used or disclosed the former employer's trade secrets; the court reasoned that an injunction was warranted because it is "impossible for [the former employee] not to disclose [the] trade secrets." *Indus. Insulation Group LLC v. Sproule,* No. 08-3482, 2009 WL 211077 (S.D. Tex. Jan. 28, 2009). Similarly, a New York federal district court found that a former employee may be enjoined from joining a competitor even before a trade secret has been disclosed because irreparable harm may be found based upon a finding of inevitable disclosure when the two employers are in direct competition and the employee possesses "highly confidential or technical knowledge concerning marketing strategies or the like." *IBM v. Papermaster*, 2008 WL 4974508 (S.D.N.Y. Nov. 21, 2008).

While California has rejected the inevitable disclosure doctrine, employers can still take measures to protect their valuable trade secrets, such as seeking injunctions or other legal remedies based on an actual or threatened trade secret violation. Given the interstate variations in trade secret law, employers should also have counsel review and routinely update confidentiality and nondisclosure agreements to ensure compliance with California or other applicable state laws. ◆

Class Action Requirements Do Not Apply to PAGA Representative Actions

Under the California Labor Code Private Attorneys General Act (PAGA), an aggrieved employee can bring a lawsuit to recover civil penalties against an employer personally and on behalf of other current and former employees for violations of the Labor Code. The employee must give written notice to both the employer and the Labor and Workforce Development Agency of the alleged Labor Code violation, along with supporting facts and theories. If the Agency fails to respond within 33 days, chooses not to issue a citation or fails to issue a citation within 158 days of the employee's notice, the employee may commence the civil action. Where civil penalties are recovered, the Agency receives 75 percent, and the remaining 25 percent goes to the aggrieved employees.

Recently, the California Supreme Court held that an aggrieved employee who brings a representative action under PAGA may recover civil penalties without satisfying class action certification requirements. In *Arias v. Superior Court*, the plaintiff alleged various wage and hour violations under the California Business & Professions Code § 17200, California's Unfair Competition Law (UCL), and claimed he was entitled to civil penalties under PAGA. The Supreme Court affirmed the Court of Appeal's decision that determined that although claims brought under the UCL are subject to class action requirements due to Proposition 64, claims under PAGA are not. The court pointed to the language of PAGA in support of its decision.

The Supreme Court disagreed with the defendant's assumption that class action requirements apply generally to any type of representative action. The court also dismissed the concern that other plaintiffs would not be bound by a PAGA finding in favor of the defendant, allowing non-party aggrieved employees to continually sue until one prevailed. The court determined that collateral estoppel would apply to all non-parties for whom the plaintiff was acting as a proxy. Thus, with respect to civil penalties, a PAGA action is akin to an action brought by the government, in which a decision would bind both the government and non-party employees.

Employers should expect that the number of PAGA claims will increase and should therefore be more vigilant in auditing their labor practices and preventing employee claims. ◆

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California Supreme Court Weighs in on Workplace Surveillance

In a ruling vindicating an employer, the California Supreme Court recently provided some helpful guidance on the permissibility of employee surveillance in *Hernandez v. Hillsides, Inc.*

Defendant Hillsides Children Center, Inc. operated a residential facility for mistreated and neglected children, some of whom had been sexually abused. It was discovered that someone was using company computers to access pornographic web sites after working hours. This understandably caused great concern for Hillsides, especially considering the nature of the facility and its goal of providing a safe environment for abused children.

Hillsides was able to trace the web traffic to two computer stations: one in the computer laboratory and one in an office shared by the two plaintiffs. Hillsides first attempted to monitor the laboratory computer using hidden video surveillance equipment, but when that proved untenable, the surveillance equipment was moved into the plaintiffs' joint office. Neither of the plaintiffs were suspected of the computer misuse, but in order to prevent word of the surveillance from reaching the perpetrator, the plaintiffs were not informed. Hillsides prevented unnecessary surveillance of the plaintiffs. The video feed was only plugged into a monitor or recording device during non-business hours and only on three occasions over a three-week period. The equipment that received the video feed was kept in a locked location and only a few people were aware the surveillance was occurring. Eventually, the plaintiffs discovered the hidden video camera and commenced an action for invasion of privacy.

The Supreme Court ruled in favor of the defendants. The court held that although the plaintiffs had a reasonable expectation of privacy in their workplace, the intrusion was not highly offensive. The court determined that while privacy expectations may be lower in the workplace, they are not nonexistent. The plaintiffs' office had both a door that closed and blinds that could be drawn down around the windows. In such an office, there is a higher expectation of privacy than in a cubical or other open working environment. However, the court held that the defendant's conduct was not highly offensive or unjustified because multiple precautions were taken to prevent surveillance of the plaintiffs. The plaintiffs were never observed or recorded, and the surveillance was limited in time and scope.

This case provides good instruction for employers considering monitoring employees. First, employers should be aware that different working conditions or facilities can affect an employee's expectation of privacy. Second, workplace surveillance may be acceptable if the employer has a legitimate purpose for the surveillance and the monitoring is limited. While the court in this case did not hold that employers must pursue the least intrusive method of surveillance, it is often the best practice. A written policy informing employees that they may be subject to surveillance is also recommended. ◆

California's New Electronic Discovery Act

California's Electronic Discovery Act became effective on June 29, 2009. The Act defines electronically stored information (ESI) and integrates the procedures for discovery of ESI into the existing rules of discovery. Among other things, the Act also allows parties to subpoena non-parties to produce ESI, requires the court to limit the extent and frequency of discovery of ESI under certain conditions, contains a procedure for information produced inadvertently and provides that a responding party may be required to translate ESI into a reasonably usable form, at the reasonable expense of the requesting party.

Employers must also remember that, immediately upon notice of pending or threatened litigation, a party becomes obligated to preserve information that may in any way be relevant to the litigation, including ESI. The Act provides that a court shall not sanction a party or its attorney for failure to provide ESI that is "lost, damaged, altered, or overwritten as a result of routine good faith operation of an electronic system."

While the Act closely parallels the December 2006 amendments to the Federal Rules of Civil Procedure, there are several differences. Most significantly, all ESI is presumed accessible under California law. An employer may object or seek a protective order in responding to a request for inaccessible ESI, but under California law, the employer must still identify the types or categories of sources of the ESI that are not reasonably accessible. Under the Federal Rules, there is no duty to produce ESI that is not reasonably accessible due to undue burden or expense.

ESI is an important and sometimes irreplaceable source of discovery and evidence in litigation. These recent amendments to the federal and state rules of discovery should be reviewed in order to properly preserve information and effectively plan and respond to discovery requests. ◆

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