Recent Trends in Arbitration and Worker Classification: What Companies Need to Know in 2020

Keith Chapman, Michael Holecek and Dhananjay S. Manthripragada

What We'll Cover…

1. AB 5 Worker Classification and Its Challengers
2. FLSA and Other Misclassification Tests
3. Arbitration (Still) Under Fire
4. Mass Arbitrations
5. PAGA and Arbitration

GIBSON DUNN

AB 5 Worker Classification and Its Challengers

History of Worker Classification

- For decades, California had a flexible independent contractor test under *S.G. Borello & Sons, Inc. v. Department of Industrial Relations*, 48 Cal. 3d 341 (1989) that considered a variety of factors, with an emphasis on the right to control the manner and means of the work performed

- The new on-demand companies brought this test into the spotlight

- In 2018, Grubhub won at trial on an individual driver's claim that he was misclassified as an independent contractor under the *Borello* test

DOORDASH

UBER

lyft

GRUBHUB

POSTMATES

Dynamex – The Court's Response

- In 2018, the California Supreme Court issued a decision in *Dynamex Operations West, Inc. v. Superior Court*, 4 Cal. 5th 903 (2018), that adopted an "ABC test" for misclassification claims brought under California's wage orders

- Under the ABC test, a hiring entity classifying a worker as an independent contractor must prove that the worker:

  - (A) Is free from the control and direction of the hiring entity (both under the contract and in fact);

  - (B) Performs work that is *outside* the usual course of the hiring entity's business; and

  - (C) Is customarily engaged in an independently established trade or business.

- The decision left open some questions, including:

  1. Would this sea change in the law be retroactive?

  2. Would it apply to claims that do not arise under the wage orders (e.g., expense reimbursement)?

AB 5 – The Legislature's Response

- AB 5 purports to codify *Dynamex*'s ABC test, but is both broader and narrower than *Dynamex*

- ***Broader***

  - AB 5 explicitly codifies the ABC test for not only wage orders but also for the Unemployment Insurance Code and the entirety of the California Labor Code

- ***Narrower***

  - AB 5 targets certain industries, but carves out a number of others

  - Challenges by groups (including journalists and ballot-signature collectors) to exclude themselves from AB 5

AB 5's Carve-Outs and Targets

Exempted Workers/Industries:

- Insurance agents
- Physicians and certain medical professionals
- Architects
- Securities broker-dealers
- Direct sales salespersons
- Real estate agents
- Licensed barbers or cosmetologists

Key Industries Not Exempted:

- On-demand app-based network companies
- Truck drivers
- Journalists

AB 5's Impact

- Companies that classify workers as independent contractors should evaluate their classifications carefully
- Potential for increase in litigation
- AB 5 gives the Attorney General, as well as large cities, the ability to bring enforcement actions for injunctive relief.
  - The AG and several city attorneys, brought such an enforcement action against Uber and Lyft on May 5.
- Pre-AB 5 Instacart lawsuit
- **But the story is still being written….**

Gig Worker Ballot Measure ("Protect App-Based Drivers and Services Act")

- Would allow app-based drivers to be independent contractors if:
  - (1) The company does not unilaterally prescribe the dates and times or hours of the driver;
  - (2) The company does not require the driver to accept any service request as a condition of staying on the platform;
  - (3) The driver can perform services for other companies; and
  - (4) The driver can work in any other occupation or business.

- Requires companies to provide certain benefits:
  - Healthcare stipend
  - Guaranteed minimum pay of at least 120% the minimum wage (with no max)
  - Reimbursement for vehicle expenses
  - Accident insurance
  - Discrimination and harassment protection

Legal Challenges to AB 5

- Trucking Industry
  - *People v. Cal Cartage Transportation Express, LLC*, Los Angeles Superior Court
    - The Los Angeles City Attorney filed enforcement actions against CCTE its sister companies and sought to enforce AB 5 through California's Unfair Competition Law.
    - On January 8, Judge William Highberger ruled that AB 5 is preempted by the FAAAA as applied to motor carriers. A writ petition challenging the ruling was summarily denied, and a petition for review by the California Supreme Court is pending.
  - *California Trucking Assn. v. Becerra*, S.D. Cal.
    - California Trucking Association filed a preemptive challenge to AB 5. On January 16, Judge Roger Benitez granted CTA a preliminary injunction, enjoining enforcement of the law by state officials as to any motor carrier operating in California.
    - On January 29, the State appealed the preliminary injunction decision to the Ninth Circuit. The appeal is awaiting oral argument.

- Journalists (*American Society of Journalists & Authors Inc. v. Becerra*, C.D. Cal.)
  - On December 17, two journalist organizations filed a challenge to AB 5's "professional services" exemption, which limits photographers and journalists to 35 freelance submissions per publication per year before they are subject to Dynamex.
  - On January 3, Judge Philip Gutierrez denied the Journalists' request for a temporary restraining order.
  - On March 20, the court denied Plaintiffs' motion for a preliminary injunction and dismissed the case.
  - On April 17, the plaintiffs appealed the decisions to the Ninth Circuit.

Legal Challenges to AB 5

- **On-Demand App-Based Network Companies (*Olson et al. v. California*, C.D. Cal.)**
  - On December 30, two gig workers, Postmates, and Uber filed a complaint challenging AB 5 as an irrational and unconstitutional statute designed to target and stifle workers and companies in the on-demand economy.
  - On February 10, Judge Dolly Gee denied Plaintiffs' motion for a preliminary injunction.
  - On March 10, Plaintiffs appealed the preliminary injunction decision to the Ninth Circuit.
  - The State has also filed a motion to dismiss, which the court announced it will decide without a hearing.
- **Court Reporters (*Williams, Weisberg & Weisberg v. California, Cal. Super. Ct. Sacramento*)**
  - On January 16, a business that provides court reporter services filed a challenge to AB 5, arguing that court reporters are not employees under the law, that its contracts with court reporters are valid and enforceable, and that the law violates the Equal Protection Clause of the California Constitution.
  - On February 26, the State filed a demurrer to the complaint and a hearing is scheduled for May 4.

GIBSON DUNN

FLSA and Other Misclassification Tests

FLSA "Economic Realities" Misclassification Test

"There is no single rule or test for determining whether an individual is an independent contractor or an employee for purposes of the FLSA." U.S. Dep't of Labor.

Courts generally look to the "economic realities" of the relationship and consider a number of factors, including:

- The nature and degree of control by the principal.
- The extent to which the services rendered are an integral part of the principal's business.
- The permanency of the relationship.
- The amount of the alleged contractor's investment in facilities and equipment.
- The alleged contractor's opportunities for profit and loss.
- The amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor.
- The degree of independent business organization and operation.

IRS 20-Factor Misclassification Test

- Instructions
- Training
- Integration
- Personal services
- Hiring, supervision, and paying assistants
- Continuing relationship
- Set hours of work
- Full time required
- Premises
- Order or sequence
  - Oral or written reports
  - Payment
  - Expenses
  - Tools/materials
  - Investment
  - Profit/loss
  - Working for others
  - Service available to the general public
  - Right to discharge
  - Right to terminate

IRS Issues New Guidance for 2020

- IRS Publication 15-A, Employer's Supplemental Tax Guide (2020) (Dec 23, 2019) announced new guidance for tax year 2020

- "Control" is primary consideration, but "20 Factor" test remains valid

- Effective January 1, 2020, the IRS will "group" factors and focus on three areas of the control test:
  - Behavior Control;
  - Financial Control; and,
  - The type of relationship of the parties.

- New reporting requirements. (*1099-NEC Nonemployee Compensation*, replaces 1099-MISC to report compensation payments to persons the employer elects to characterize as independent contractors.)

GIBSON DUNN

Arbitration (Still) Under Fire

History of Arbitration

- The United States Supreme Court has repeatedly held that arbitration must not be viewed with hostility
- Over the past decade in particular, the Court has issued a number of decisions protecting individual arbitration under the FAA
  - *Stolt-Nielsen S.A. v. AnimalFeeds International* (2010)
  - *AT&T Mobility LLC v. Concepcion* (2011)
  - *American Express Corp. v. Italian Colors Restaurant* (2013)
  - *Epic Systems Corp. v. Lewis* (2018)
  - *Lamps Plus, Inc. v. Varela* (2019)
- **States, however, continue to fight these decisions…**

AB 51 – Arbitration Provisions in Employment Agreements

- **No mandatory arbitration agreements** as a condition of employment for new hires, applicants, or existing employees
  - Employees cannot be required to waive any right, forum, or procedure under FEHA, the Labor Code, or other statutes governing employment.
- **An opt-out is not sufficient** and will still result in liability
- **No retaliation or discrimination** against an applicant or employee who refuses to sign an agreement that would violate this section
- **Civil and criminal penalties** for employers who violate this section

AB 51's Limitations

- Negotiated severance agreements
- Post-dispute settlement agreements
- Agreements entered into, modified, or extended prior to January 1, 2020
- Agreements that are enforceable under the Federal Arbitration Act

AB 51 Enjoined – *Chamber of Commerce v. Becerra* (E.D. Cal.)

- On December 30, 2019, Judge Kimberly Mueller issued a temporary restraining order enjoining the enforcement of AB 51
- The challenge to AB 51 was filed by the United States Chamber of Commerce and argues that AB 51, even with the carve-out, is preempted by the FAA
- On January 10, the Court issued preliminary injunction (Feb. 7 written order). Injunction applies to all arbitration agreements covered by the FAA
- February 29: the State filed its Notice of Appeal

SB 707 – Payment of Arbitration Fees

- If employer fails to pay those fees and costs within 30 days of the due date, employer is in:
  - (1) Material breach of arbitration agreement,
  - (2) Default in arbitration, and
  - (3) ***Waives its right to compel arbitration***.
- Employee would then have option to proceed in court or compel arbitration with employer to pay attorneys' fees and costs
- Law gives more leverage to plaintiffs' firms pursuing mass arbitrations because of the steep penalties for employers that fail to pay
- Preempted by the FAA?

GIBSON DUNN

Mass Arbitration

Mass Arbitrations

- Certain plaintiffs' firms have also tried to avoid the wealth of pro-arbitration precedent from the Supreme Court by filing mass individual arbitrations on behalf of a large number of clients
- Because arbitration agreements sometimes require companies to pay arbitration fees, these firms demand that the companies pay millions in such fees
- SB 707 imposes sanctions on companies that do not pay these fees when invoiced by the arbitration provider.
    - Potential Defenses – Enforcing individual arbitration requirements; exposing lack of attorney-client relationship; challenging SB 707.
    - Proactive Measures – Strengthening arbitration agreements.

GIBSON DUNN

PAGA and Arbitration

PAGA and Arbitration

- Status of *Iskanian* rule after *Epic Systems*
  - *Correia v. NB Baker Elec., Inc.*
  - *Zakaryan v. Men's Wearhouse, Inc.*
- *ZB v. Superior Ct. (Lawson)*
- *Kim v. Reins* (March 15, 2020)
- Claims for public injunctive relief

GIBSON DUNN

Professional Profiles

Michael Holecek

333 South Grand Avenue
Los Angeles, CA 90071-3197 USA
Tel +1 213.229.7018
MHolecek@gibsondunn.com

Michael Holecek is a partner in the Los Angeles office of Gibson, Dunn & Crutcher, where his practice focuses on complex commercial litigation both in the trial court and on appeal. He has first-chair trial experience and has successfully tried to verdict both jury and bench trials. He has also argued numerous appeals to the California Court of Appeal, including *Rodriquez v. Menjivar*, 243 Cal. App. 4th 816 (2015), and *Jaime G. v. H.L.*, 25 Cal. App. 5th 794 (2018), in which he obtained complete reversals of adverse trial court rulings for his client, in published opinions. He has also authored articles on appellate procedure, civil discovery, corporate appraisal actions, data privacy, and bad-faith insurance litigation.

In 2017, Mr. Holecek was selected by the Carl & Roberta Deutsch Foundation as a 2017 HALO Award winner for his work on behalf of domestic-violence survivors. He was also honored as a winner of Gibson Dunn's Frank Wheat Memorial Award for his commitment to pro bono work.
Mr. Holecek serves on the Board of Directors of Family Violence Appellate Project, a nonprofit organization dedicated to providing free legal representation to domestic violence survivors.

Mr. Holecek earned his law degree with high honors from the University of Chicago Law School in 2011. While at Chicago, he was a member of the *University of Chicago Law Review*. Mr. Holecek was runner-up in the Hinton Moot Court Competition and winner of the Karl Llewellyn Cup and the Thomas R. Mulroy Award for Excellence in Appellate Advocacy. He was a Kirkland & Ellis Scholar and was elected to the Order of the Coif.

Mr. Holecek graduated *magna cum laude* from Rollins College in 2001 with a bachelor's degree in Political Science and a minor in Fine Art.

Before attending law school, he founded and served as Managing Director of ERA Real Estate, the second largest residential real estate network in the Czech Republic.

Mr. Holecek is admitted to practice in the State of California.

Dhananjay S. Manthripragada

333 South Grand Avenue
Los Angeles, CA 90071-3197 USA
Tel +1 213.229.7366
DManthripragada@gibsondunn.com

Dhananjay Manthripragada is a partner in the Los Angeles office of Gibson, Dunn & Crutcher and was formerly with the firm's Washington, D.C. office, resulting in a broad complex litigation practice that is truly national in scope. He is a member of the firm's Litigation, Class Actions, and Government Contracts Practice Groups, and leads the firm's Aerospace & Related Industries industry group. Mr. Manthripragada has extensive experience defending companies in complex litigation in state and federal courts throughout the country, from pre-trial demands through trial, arbitration, or settlement, and on appeal. He has represented some of the world's leading defense, high-technology, consumer products, food and beverage, pharmaceuticals, chemicals, and automotive companies in their most significant matters.

Mr. Manthripragada has served as counsel in a range of employment, consumer, wage-and-hour, antitrust, unfair competition, and environmental class action and derivative lawsuits.

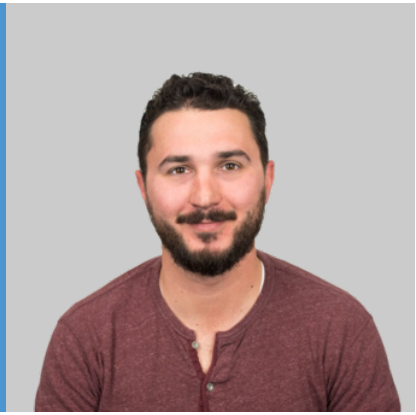
Mr. Manthripragada has significant experience on a broad range of government contracts issues, including civil and criminal fraud investigations and litigation, complex claims preparation and litigation, cost allowability, and the Cost Accounting Standards. He has represented government contractors before the Armed Services Board of Contract Appeals in numerous appeals, and has provided advice to clients on issues involving contract negotiations, claims analysis, and contract performance.

In addition, Mr. Manthripragada has maintained a consistent dedication to providing pro bono representation, particularly focused on cases relating to immigration, transition-aged foster youth and human trafficking. He has been recognized by various organizations, including the Bay Area Legal Aid Foundation, for his efforts.

Mr. Manthripragada received a law degree in 2007 from the University of California, Los Angeles, where he served as Chief Comments Editor and Articles Editor of the *UCLA Journal of Environmental Law & Policy*. While in law school, Mr. Manthripragada served as a judicial extern to Judge Kim McLane Wardlaw of the U.S. Court of Appeals for the Ninth Circuit. He graduated *magna cum laude* with a Bachelor of Arts degree in Biology from Duke University in 2004. Mr. Manthripragada is admitted to practice law in the District of Columbia and the state of California.

R. Keith Chapman

201 3rd Street, Suite 200
San Francisco, CA 94103 USA
Tel +1 415.857.4646
Keith@Postmates.com



R. Keith Chapman is an Associate General Counsel for Postmates Inc. He manages legal teams that oversee litigation, public policy, employment, trust & safety, insurance, and risk. Working at the forefront of future-of-work topics, Chapman helps Postmates lead legislative and labor outreach across the country and at the national level.

Prior to joining Postmates in 2016, Chapman counseled and defended employers as an attorney with Littler Mendleson, P.C., in San Francisco, with practice areas focused on the gig-economy, wage & hour class action defense, and anti-discrimination. Chapman has also served as a managing attorney with the New York City Commission on Human Rights and clerked for the United Nations International Criminal Tribunal for Rwanda at the Trial Chambers, in Arusha, Tanzania, and Appellate Chamber, in the Hague, Netherlands.

Chapman received his J.D., with Honors, from Rutgers University in 2005.