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Employer's Right to Settle Disputed Claims with Individual Employees Affirmed

By Jody A. Landry and Justin A. Morello

The California Court of Appeal recently affirmed an employer's right to settle a putative class member's disputed wage claims individually, without the consent or involvement of class counsel. In *Chindarah v. Pick-Up Stix*, the appellate court affirmed the trial court's order that enforced the settlement and release agreements signed by more than 200 putative class members (many of whom later joined the lawsuit as named plaintiffs) and granted summary judgment for the company on those plaintiffs' wage claims.

Factual Background

In July 2003, two former Pick-Up Stix employees amended their individual complaint to allege a putative class action against their former employer. Through the amended complaint, the plaintiffs alleged Pick-Up Stix misclassified its current and former general managers, assistant managers, and lead cooks as exempt employees. After a failed mediation, Stix began settling the misclassification claims with as many individual putative class members as possible. Stix offered the individual putative class members an amount based upon a figure Stix previously offered in mediation. More than 200 former and current employees accepted the offer and signed a settlement agreement that contained a general release.

The settlement agreement also required that the signing employee acknowledge that he or she had spent more than 50% of his or her time performing managerial duties, released Stix from all claims for unpaid overtime and any other California Labor Code violations during the putative class period, and agreed "not to participate in any class action that may include ... any of the released Claims."

In response, the original plaintiffs filed a second amended complaint that alleged the settlement agreements violated numerous provisions of the Labor Code. Through the amended complaint, eight current and former Stix employees who had signed the settlement agreements joined the putative class action as named plaintiffs. Stix filed a cross-complaint against the new plaintiffs that alleged breach of contract and breach of the settlement agreements, and sought declaratory relief.

The parties filed cross motions for summary judgment. The plaintiffs claimed the releases they signed were void under Labor Code sections 206 and 206.5. Stix claimed the releases barred recovery by the plaintiffs who had signed the releases and settlement agreements.

The trial court found that the releases were enforceable because the Labor Code did not prohibit the release of wage claims where there is a "bona fide dispute" over whether "any wages were owed." Stix produced evidence showing a good faith dispute with regard to the classification of employees and thus created a triable issue of fact as to whether the putative class members were owed any additional wages. Because the releases were enforceable, the trial court granted Stix's motion for summary judgment and denied the plaintiff's motion.

The Appellate Court Affirms the Trial Court's Ruling and Holds Wage Claims May Be Released Where a Bona Fide Dispute Exists Regarding Whether the Released Wages Are Owed

The plaintiffs argued the releases could not be enforced because sections 206, 206.5, and 1194 prohibited any settlement of a dispute over overtime compensation. The plaintiffs argued that sections 206 and 206.5 were enacted to protect employees from employers who attempt to coerce a settlement by withholding wages. They urged the court to ignore, as *dicta*, language in case law[1] interpreting sections 206 and 206.5 to allow the compromise and release of a bona fide dispute over wages. They argued that the plain language of section 206.5 voided the release of all "wages due, or to become due" and therefore included the release of disputed wages because those disputed wages could eventually be found to be owed. The plaintiffs also argued that the court should consider case law[2] interpreting the Federal Labor Standards Act (FLSA) to prohibit employees from obtaining the release of disputed wage claims even though the FLSA provides no express prohibition of such releases. Finally, the plaintiffs argued that because the right to overtime compensation was an unwaiveable right it could not be settled.[3]

The California Court of Appeal rejected each of these arguments. It first noted that the legislative history of section 206.5 showed it was enacted to ensure employers could not obtain a release of all claims, write a bad check, and then prevent recovery of owed wages by pointing to the signed release. The legislature did not enact section 206.5 because of any perceived coercion regarding the settlement of a disputed wage claim. Thus, the court rejected the plaintiffs' argument that the release of disputed wage claims was coercive and grounds to invalidate the settlement and release agreements.

Next, the court acknowledged that there were no California cases directly on point; however, federal courts[4] applying California law did cite *Reid v. Overland Machined Products*[5] and *Sullivan v. Del Conte Masonry Co.*[6] to uphold the release of disputed wage claims. Those courts held that wages are not due if there is a good faith dispute as to whether they are owed. The court ultimately found those cases to be persuasive as it reached the same conclusions.

The appellate court dispatched the plaintiffs' analogy to the FLSA by noting the lack of statutes or case law requiring court approval of private wage settlements showed there was no basis for such a requirement to be read into California law. Indeed, the court noted the California Legislature is capable of requiring such review: Labor Code section 5001 bars any compromise or release of workers' compensation claims without the approval of the workers' compensation appeals board. But the legislature did not enact a similar provision for wage claims.

Finally, the court rejected the plaintiffs' argument that the release of disputed wage claims somehow violated public policy because such a settlement would require the waiver of the employee's right to overtime by noting that "there is no statute providing that an employee cannot release his claim to past overtime wages as part of a settlement of a bona fide dispute over those wages." The court held that public policy is not violated by a settlement of a bona fide dispute over wages already earned. The releases settled a dispute over past wages and did not exonerate Stix from future violations. The releases also did not condition the settlement on the payment of wages concededly due at the time of their execution.

Thus, the court held that the trial court correctly found the releases were enforceable and barred the plaintiffs from proceeding with the lawsuit against Stix.

The Take Away

At the outset, employers should note that *Chindarah* arises out of *pre-certification* settlement and release agreements with individuals who were not represented by counsel at the time. Once a class has been certified and the opt-out or opt-in period has elapsed, the class members are deemed to be represented by counsel. Furthermore, employers should be aware that they may not settle individual claims under the FLSA for the same wages without court or administrative approval by the Department of Labor. As a result, employers who settle only California wage claims, as *Chindarah* permits, may find they still are facing claims under federal law for the same wages.

Employers who are considering settling with individual *putative* class members should consider three issues:

1. How will the settlement and release be structured?
2. How will a bona fide dispute be shown?
3. How will the releases be obtained?

Chindarah provides employers with some guidelines regarding how releases in settlement and separation agreements should be structured. If the employer wishes to include the release of wage claims, the settlement should:

- Separately acknowledge receipt of all wages due (including all forms of wages such as accrued and unpaid vacation, earned commissions, earned bonuses, etc.);
- Note that the employee would not be entitled to any compensation paid under the agreement if the employee did not provide the stated release; and
- Note that the settlement and release of wage claims relates to disputed wages.

Employers should consider how a "bona fide dispute" over wages that are the subject of the release will be shown. One method, used in *Chindarah*, would be to have the employee specifically acknowledge a factual basis for the dispute. In *Chindarah*, the employees signing the releases specifically acknowledged that they spent more than 50% of the time performing managerial duties during the alleged class period, thus creating a dispute over whether they were misclassified as exempt.

Notably absent from the *Chindarah* opinion is a discussion of how the releases were obtained. Instead, the court simply noted that after the mediation failed, "Stix then decided to attempt settlement with as many putative class members as possible." The mere fact the releases were obtained shows that *Chindarah* affirms the right of an employer to speak directly with its employees regarding a pending class action, contest the claims raised in the action, and offer putative class members money to settle their claims that would be part of the class action; all without the consent or involvement of class counsel.

Employers should expect that when class counsel learns that settlement agreements are being offered without counsel's involvement, they may seek an injunction preventing further communications between the employer and the putative class members. Later, class counsel may attack those settlement agreements by arguing that they were obtained through coercion. Thus, employers considering settlement with individual putative class members should develop a protocol to ensure that their right to communicate with their current and former employees and to resolve potentially disputed claims without interference from class counsel is preserved. Employers should keep in mind general guidelines for communicating with putative class members regarding ongoing litigation. Any statements to putative class members should: (1) be truthful and not misleading; (2) confirm that any opinions are the company's own opinions and not legal advice or the opinion of the court; and (3) confirm that it is the employee's choice whether to sign the agreement. Employers should refrain from making any communication that could be interpreted as discouraging employees from participating in the lawsuit.

Jody A. Landry is a Shareholder and Justin A. Morello is an Associate in Littler Mendelson's San Diego office. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com, Ms. Landry at jlandry@littler.com, or Mr. Morello at jmorello@littler.com.

[1] *Reid v. Overland Machined Prods*., 55 Cal. 2d 203 (1961); *Sullivan v. Del Conte Masonry Co*., 238 Cal. App. 2d 630 (1965).

[2] *Lynn's Food Stores, Inc. v. U.S*., 679 F.2d 1350, 1352-53 (11th Cir. 1982); *but see Martinez v. Bohls Bearing Equip. Co*., 361 F. Supp. 2d 608 (W.D. Texas 2005).

[3] Citing *Edwards v. Arthur Anderson*, 44 Cal. 4th 937 (2008) (employee cannot release his nonwaivable right to indemnity).

[4] *Reynov v. ADP Claims Servs. Group, Inc*., No. C 06-2056 CW, 2007 WL 5307977 (N.D. Cal. 2007); *Kelly v. City & County of S.F*., No. C 05-1287 SI, 2008 WL 2662017 (N.D. Cal. 2008); *Jimenez v. JP Morgan Chase & Co*., No. 08-CV-0152W(WMC), 2008 WL 2036896 (S.D. Cal. 2008).

[5] 55 Cal. 2d 203.

[6] 238 Cal. App. 2d 630.