THE BKCG
BULLETIN
SPRING 2014 EDITION

Does Your Company Have A Viable Electronic Monitoring Policy In Place?

In the modern workplace, the necessity of pervasive internet use and e-mail communications is universal. As a result, it is increasingly commonplace for employers to implement specific policies that either limit or prohibit the use of company devices for personal electronic activities. In order to police such use, these policies often provide the employer with the right to monitor and review its employees' use of company telephones and computers, implicating various privacy-related concerns. Although the state of the law on this topic continues to evolve and varies from state to state, an employer can generally defeat its employees' reasonable expectation of privacy in electronic activities conducted on company devices if: (1) the policy is sufficiently specific as to the monitored activities at issue, and (2) the employee has actual notice of the policy.

For example, the California Court of Appeal held that an employee had no reasonable expectation of privacy in the information stored on his home computer which was purchased by the company for business-related purposes. *(TBG Ins. Services Corp. v. Superior Court (2002) 96 Cal.App.4th 443.)*

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If Your Business Is A Franchise, Make Sure You Get This Right

If your business has a vertical distribution chain, licenses your trademarks to others, or retains commissioned sales agents to sell your goods or services, a franchise model presents a number of distinct advantages to expand your market and develop the strength of your brand while reducing your own investment risk and costs. The disadvantage to this is that franchises are highly regulated under federal and state law.

But what if you do not intend to be a franchise business?

Whether your business model is a "franchise" often involves a significant amount of gray area under federal and state franchise laws. This can result in a finding that your business is a "franchise" as a matter of law, regardless of your intent.

Unfortunately, the consequences of having an "unintended franchise" in this way can be devastating for you and your business. For example, violation of California State franchise laws can make your management and owners subject to individual liability regardless of your business's status as a separate legal entity, or can even result in criminal liability.

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Does Your Company Have A Viable Electronic Monitoring Policy In Place?

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The Court's holding hinged on the employer's stated policy which required the employee to use the computer "for business purposes only and not for personal benefit or non-Company purposes." The employee consented to this policy which also allowed the employer to monitor the information on the computer on an "as needed" basis. Thus, the employee "fully and voluntarily relinquished his privacy rights in the information he stored on his home computer."

In another recent example of the breadth of a properly implemented electronic monitoring policy, the Court of Appeal in *Holmes v. Petrovich Development Co.* (2011) 191 Cal.App.4th 1047 found that not even electronic communications between an employee and her attorney were protected because the employee used her company e-mail account and computer. The operative company policy specifically advised the employee that "the company's technology resources should be used only for company business and that employees are prohibited from sending or receiving personal e-mails." It also warned that "employees who use the Company's Technology Resources to create or maintain personal information or messages have no right of privacy with respect to that information or message."

Conversely, the Supreme Court of New Jersey arrived at a different result when it found that an employee retained an expectation of privacy in attorney-client communications transmitted via a company computer because she used a personal web-based e-mail account. *Stengart v. Loving Care Agency, Inc.* (2010) 201 N.J. 300. The *Stengart* Court found that the "general language" of the policy which prohibited the use of company "media systems and services" for personal use, did not defeat the employee's reasonable expectation of privacy in the communications at issue because the policy did not specifically address the use of personal, web-based e-mail accounts.

Further complicating each of these issues is the increasing number of employees using *their own* electronic devices to conduct company business. Because most employees access company servers with their personal devices, this implicates new concerns regarding specific "BYOD" (bring your own device) policies and the balance between the scope of an employee's expectation of privacy and an employer's interest in the protection of valuable company information. Thus, increasing numbers of companies are employing specific "BYOD" policies to address these specific concerns. Below are a few general considerations that any employer should address in its BYOD policy:

- **Mandate A Security Policy For All Devices:** Many employees choose not to password protect their personal electronic devices in the interest of convenience. This puts sensitive company information at risk, despite the availability of simple measures to protect the integrity of the information on the device;

- **Define The Relative Ownership Of Information On The Device:** The policy should set forth guidelines as to an employer's right to wipe company devices in the event the device and information contained therein is compromised; for example, if the device is lost or stolen. Because this puts personal employee information at risk, the policy should address the employee's responsibility to secure and backup the information on the device in the event the employer is required to wipe the device to protect sensitive company information;

- **Define An Acceptable Use Policy For The Device:** Certain applications may present greater security risks than others, and the employer should make itself aware of questionable applications that should be prohibited on any device;

- **Develop An Exit Strategy:** The employer should have procedures in place when employees separate from the company to protect company information still stored on the employee's device.

Ultimately, an employer needs to implement clear written policies, acknowledged by the employee, that address the employee's relative privacy rights on both company-owned and employee-owned electronic devices, and the employer's right to protect company information. The employer must also consider the extent to which it should police employee electronic activities at the potential risk of employee productivity and mistrust.

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If Your Business Is A Franchise, Make Sure You Get This Right

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So what is a franchise and how do you know if your business is classified as one?

There are two areas of regulatory authority governing this—federal law (which is governed by the FTC Franchise Rule set forth in 16 C.F.R. 436), and state franchise laws, most of which are similar to the "FTC Rule" and add their own additional regulations.

The FTC Rule

The FTC Rule defines a "franchise" as any continuing commercial relationship or arrangement, whatever it may be called, in which the terms of the offer or contract specify, or the franchise seller promises or represents, orally or in writing, that:

(1) The franchisee will obtain the right to operate a business that is identified or associated with the franchisor's trademark, or to offer, sell, or distribute goods, services, or commodities that are identified or associated with the franchisor's trademark;

(2) The franchisor will exert or has authority to exert a significant degree of control over the franchisee's method of operation, or provide significant assistance in the franchisee's method of operation; and

(3) As a condition of obtaining or commencing operation of the franchise, the franchisee makes a required payment or commits to make a required payment to the franchisor or its affiliate. (16 C.F.R. 436.1(h)).

California Law

The California Franchise Investment Law's (the "CFIL") definition of "franchise" has some slight variations from the FTC Rule. The CFIL defines a "franchise" as a contract or agreement, either expressed or implied, whether oral or written, between two or more persons by which:

1) A franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services under a marketing plan or system prescribed in substantial part by a franchisor;

2) The operation of the franchisee's business pursuant to such plan or system is substantially associated with the franchisor's trademark, service mark, trade name, logotype, advertising, or other commercial symbol designating the franchisor or its affiliate; and

3) The franchisee is required to pay, directly or indirectly, a franchise fee. (California Corporations Code section 31005).

Statutes in other states have even broader definitions of "franchise" than California's CFIL, and it is important to understand these differences when doing business with persons or entities located outside of California.

So what if your business falls under the definition of a franchise?

Falling under the definition of "franchise" under federal or state laws imposes additional regulations and obligations on your business, as well as your agreements with others. This can significantly affect the way you do business and expose you to liability if you are not careful.

For example, most states, including California, place restrictions and limitations on the termination or nonrenewal of franchise agreements. In some states, these restrictions can effectively change a licensing agreement that was otherwise terminable at-will into a franchise agreement that requires "good cause" for termination.

While California is not a "good cause" state, the differences in franchise laws from state-to-state further underscore the importance of knowing the franchise laws of every jurisdiction in which you do business. In addition, most state franchise laws do not enable you to "contract around" their applicability merely by inserting choice of law or waiver provisions in your agreements.

If you believe your business involves more than one of the elements of a "franchise" in the FTC Rule or CFIL definitions described above, be sure to make a careful inquiry into your business model to determine if these laws apply to you to avoid being entangled in potentially costly legal trouble as an "unintended franchise."

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Tired of Frivolous Wage Claims From Former Employees? A New California Ruling Can Help . . . Maybe

As most employers in California know, employees in this state enjoy a relatively quick and inexpensive means to pursue their claims for unpaid wages (or vacation pay, etc.) by utilizing the Labor Commissioner's Division of Labor Standards Enforcement (DLSE) administrative hearing process. In theory, this process provides valuable safeguards for employees to ensure they are receiving their promised compensation. In practice, however, all too often, unscrupulous or disgruntled former employees misuse this process to gain undue advantage over an employer acting perfectly legitimately. Not surprisingly, sophisticated employers have sought to limit this potential abuse by having their employees sign broad employment arbitration agreements. Well-crafted arbitration agreements often include a waiver of not only jury trials, but DLSE hearings as well. For years, however, California courts have held that any attempt to have an employee waive its right to these DLSE hearings (known as "Berman" hearings) will not be enforced. With a recent ruling from the California Supreme Court, that is changing—maybe.

In 2011, the United States Supreme Court issued a landmark decision regarding arbitration agreements known as *Concepcion (AT&T Mobility LLC v. Concepcion* (2011) 131 S.Ct. 1740). In sum, the Supreme Court ruled that states (such as California) cannot impinge on the right to arbitrate because that is exclusively the purview of the Federal Arbitration Act (FAA). Since the *Concepcion* ruling, the effects continue to ripple across the legal landscape, especially in the employment context. This ripple effect has now cascaded onto the issue of Berman hearing waivers. On October 17, 2013, the California Supreme Court handed down its opinion in *Sonic-Calabasas A, Inc. v. Moreno (Sonic II)*. In *Sonic II*, the California high court attempts to reconcile the California courts' apparent predisposition to prevent waivers of Berman hearings with the clear instruction of *Concepcion* that states cannot interfere with lawful arbitration agreements.

The facts of Sonic II are not atypical. The plaintiff, Frank Moreno, was an employee of a Sonic car dealership. After he quit, he filed a claim with the DLSE for vacation pay and labor code penalties. When Sonic filed court papers to block the Berman hearing based on a well written arbitration agreement, the trial court denied Sonic's request, holding that Sonic could go to arbitration after the Berman hearing if it did not like the DLSE's decision. Sonic appealed, and the court of appeal reversed. The California Supreme Court in Sonic I, then held that, as a "categorical rule", an employer cannot require an employee, as a condition of employment, to waive the right to a Berman hearing. The United States Supreme Court ultimately chimed in, holding that the California Court must reconsider in light of the Concepcion ruling.

Now, in Sonic II, the Court acknowledges that its previous bright-line rule barring Berman waivers is not allowed. Unfortunately, however, the Court left plenty of room for ambiguity. The Court ruled that the employee can still try to show that the arbitration agreement is unconscionable, but failed to set out a clear test for that. Cynically, this can be viewed as California's way of continuing to permit attacks on arbitration agreements. Indeed, as stated by the dissenting justice, the majority has formulated " yet another device for for invalidating arbitration agreements: a case-by-case, hopelessly vague, subjective, and indeterminable assessment of (1) the value of the benefits of the Berman procedure to a particular employee, and (2) the accessibility and affordability to that employee of the specific arbitration procedure to which he or she has agreed. The majority's approach is inconsistent with California law and is preempted by the FAA."

The upshot? A sophisticated employer should continue to utilize well-crafted, broad arbitration agreements. But, keep us on your speed dial. That is certainly no guarantee that you will be staying out of the courtroom in California.

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The Truth About Non-Competes Under California Law

Few contractual rights are as misunderstood in California as covenants not to compete, i.e., contractual provisions in employment agreements that prohibit or restrict an employee from competing with his or her employer after the employment relationship terminates. Many uninformed employers assume that non-compete covenants will provide legal redress should its employee leave the company to form a competing enterprise and employees often assume the non-compete covenants will result in liability should they lure away their former employer's clients.

The truth is that under most circumstances, a California court will not enforce a covenant not to compete. Section 16600 of the Business & Professions Code provides in pertinent part that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." Courts have developed case law interpreting this statute, and this precedent has grown increasingly protective of an employee's rights to freely compete with his or her employer, regardless of any covenant purporting to restrict the employee's rights to compete with the former employer.

Under the current state of the law in the employment context, the only circumstance in which a Court will enforce a covenant not to compete against a former employee is if that former employee used confidential or trade secret information obtained during the employment to unfairly compete with his or her former employer. While this rule may sound clear enough at first blush, significant uncertainty remains concerning what, exactly, constitutes "confidential" and "trade secret" information. In addition, employers can increase the likelihood that a Court will enforce a non-compete covenant in its particular circumstance if that employer includes necessary language in its employment agreement and takes the requisite actions.

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Employee Handbooks, Don't Just Issue And Forget About It

At this point, most savvy California employers have an Employee Handbook (if you don't, please call us!). However, many employers mistakenly believe that once their Employee Handbook has been created, that's one less thing to worry about and they can forever cross it off their "to do" list. Unfortunately, this practice is ill-advised, as employment laws are not static and neither are trends in employment litigation directed at employers' employment practices.

California's Unfair Business Practices Act, Business & Professions Code Section 17200 et seq. allows an employee to file a civil lawsuit against an employer for virtually *any* violation of an employment law, including oversights which are entirely inadvertent or seemingly trivial. This statute has spawned a virtual cottage industry of plaintiffs' contingency employment lawyers, who aggressively advertise in mass circulation publications and online seeking disgruntled employees they can turn into litigants, worse yet, representative plaintiffs in class actions, which are lawsuits filed on behalf of every employee who was allegedly treated the same way as the class plaintiff.

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New California LLC Act Took Effect January 1, 2014

If you are considering becoming a member or a manager of a California limited liability company (LLC), or are already a member or manager of a California limited liability company formed prior to 2014, you should be aware that California's Revised Uniform Limited Liability Company Act (RULLCA) took effect on January 1, 2014 and replaced the Beverly-Killea Limited Liability Company Act which has governed the operation of California LLCs since their inception in 1994. As well as applying to all California LLCs formed or foreign LLCs registered with the California Secretary of State on or after January 1, 2014, RULLCA's default rules will also "fill in the blanks" in the Operating Agreements of all LLCs formed or registered in California prior to 2014. California joins 7 other states and the District of Columbia that have enacted RULLCA, but the new law reaffirms the differences with Delaware's Limited Liability Company Act (Delaware Act). Of particular note in this regard are the following: (1) the limitations that RULLCA places on an LLC's ability to permit the waiver of fiduciary duties of a member in a member-managed LLC, or a manager in a manager-managed LLC; and (2) the fact that, under RULLCA, a creditor with a judgment against a member of a California LLC formed on or after January 1, 2014 will now be able to foreclose on the creditor's judgment lien against the member's membership interest in the LLC, if the creditor can show that distributions from the LLC will not be sufficient to pay the judgment debt within a reasonable time. In both of these regards, RULLCA varies dramatically from the Delaware Act. A more in-depth article on RULLCA and its significance will appear in a forthcoming issue of the BKCG Bulletin.

Employee Handbooks, Don't Just Issue And Forget About It

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Here is a verbatim quote from just such an advertisement one of our clients recently brought to our attention:

> *"Recent case law has made CLASS ACTIONS suitable for these cases. We are NOW selecting CLASS REPRESENTATIVES.*
> ***If you are selected you may also receive a special fee from the court of upto $25,000, in addition to your losses."***

A "class" can consist of dozens, hundreds or even thousands of past *and* present employees whose alleged claims may, in the aggregate, total six figures or more!

Regular review of your Employee Handbook will ensure that you stay on top of employment law changes that could expose your business to significant liability and can also offer you tools to help manage your potential exposure. For example, within the last year, the United States Supreme Court and the California Court of Appeal have handed down rulings suggesting that employers may now be able to protect themselves against employee class action lawsuits through the use of carefully drafted arbitration agreements containing class action waivers. Please see the article on page 8 of this edition of the BKCG *Bulletin*. The law in this area is still evolving and will undoubtedly be the subject of a future article in the BKCG *Bulletin*.

For additional information, questions or comments on these articles, or any other employment-related or LLC-related matters please contact Greg Clement at gclement@bkcglaw.com or 949-975-7586.

Employer Best Practices

In 2012, California employees filed a staggering 19,839 lawsuits against their employers alleging some form of discriminatory conduct under the Fair Employment and Housing Act ("FEHA"). That figure represents a 10% increase over 2011, with some of the largest increases coming in the age or disability based wrongful termination (or reduction in force) categories. According to the 2012-2013 Edition of Jury Award Trends and Statistics, the nationwide median jury award for age cases was $247,800, and was $292,500 for disability claims. As the number of cases increases, so too does the median cost of settlement, which was over $100,000, according to the most recent national data.

Being sued by a former employee does not, however, mean that the sky is falling. In fact, the national statistics show that these claims are successful at trial less than half of the time, and in California, employers can challenge the validity of a wrongful termination claim before trial with a summary judgment motion. To win this motion, the employer must produce admissible evidence of a *legitimate, nondiscriminatory reason* for the termination. If the employer can sustain this burden, the plaintiff can only avoid summary judgment by presenting admissible evidence showing that the employer's stated reason for the termination was actually just a pretext. If the employee cannot meet that burden, the court should grant the summary judgment motion and dismiss the wrongful termination claim.

Producing admissible evidence of a *legitimate, nondiscriminatory reason* for the termination sufficient to prevail on summary judgment can be difficult, if not impossible, for the unprepared employer. As a prepared employer, however, you can marshal this evidence long before the termination decision even arises by implementing the following procedures:

- Clearly define performance standards, objective responsibilities and requirements for each position. Objective criteria and mandatory skills are easier to demonstrate and enforce than subjective qualities and characteristics.

- Clearly document all hiring decisions. Encourage your hiring personnel to take notes during interviews relating to the objective responsibilities and requirements established for the position, and keep those notes in a safe place.

- If an employee is counseled on a performance-related issue by a supervisor, even it is does not rise to the level of a formal "write-up", make sure the issue is documented in the employee's personnel file with a brief, neutral factual summary of the issue and the counseling provided.

- Adopt an equitable and uniform format and policy for administering performance evaluations. Conduct evaluations on a regular basis and ensure that they are easily documented. Moreover, make sure that your supervisors are aware of the importance of documenting employees' performance honestly and accurately.

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Is Your Company Doing What It Can To Protect Itself From A Class Action?

Becoming the target of a Class Action can decimate any company. In California, where staying abreast and in compliance with ever-changing laws is challenging to say the least, adding an arbitration provision to your contracts that includes a class action waiver could be a valuable measure of protection. In other words, by forcing the suing party to arbitrate, you prevent them from pursuing class action claims thereby substantially limiting your company's exposure. The caveat is that the arbitration provision itself must be carefully drafted to be enforceable. For example, a Court might refuse to enforce your arbitration provision if it decides the provision is too one-sided and favors the company or if the provision is not obvious enough to the person reading the contract. If you cannot get the case into arbitration, your company loses the benefit of any class action waiver. These arbitration provisions with class waivers have already proven to be extremely beneficial in employment and consumer contracts but could also provide added protection in other types of contracts. For this reason, every company should have an attorney review the contracts it routinely uses for two reasons; (1) to see if an arbitration provision with a class waiver could benefit the company and, (2) to ensure the arbitration provision will likely be enforced in the unfortunate event the company is targeted as part of a class action.

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Employer Best Practices

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- Before making a decision to terminate as part of a workforce reduction, verify that the employee is aware of all performance standards, objective criteria and requirements upon which his or her performance is being evaluated.

- In a reduction of force, be prepared to demonstrate that retention decisions were not based on the protected class of any individual and did not have discriminatory intent. If members of a protected class (e.g., employees over the age of 40) are being eliminated as part of the workforce reduction, you must be prepared to demonstrate how and why age was not a factor in the firing decision. Similarly, you can use statistical data to your advantage by showing that the reduction in force impacted all employees equally.

- Consider offering severance packages, outplacement counseling and letters of recommendation to employees impacted by a reduction in force in exchange for a release of claims.

The statistics show that employers with 100 or more employees can expect a termination-related claim at least once every three years. Even the best practices cannot ensure that you will not be sued by a jilted former employee. But by establishing and implementing objective standards, you can arm your company with evidence of the legitimate and nondiscriminatory reasons it will need to defend against the growing tide of discrimination-based claims.

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