

The logo for Fisher Phillips, featuring the company name in white text on a red, angular background.

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# A New Wave in Workplace Law

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# Managing, Calculating and Internally Communicating Risk Stemming from the New Tsunami of PAGA Lawsuits in California

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# Introduction

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The business community has seen a significant spike in the number of cases brought, under the California Labor Code's Private Attorneys General Act of 2004 ("PAGA"), over the past five years. Statistics show that there has been an average eight to ten percent increase in the number of PAGA administrative complaints filed with the California Labor Workforce Development Agency ("LWDA") and/or in court.

The increase is a result of multiple trends including, but not limited to: 1) implementation and enforcement of pre-dispute arbitration agreements with class-action waiver; 2) increased difficulty in certification of class action lawsuits where there is no such requirement in PAGA cases; 3) avoidance of Rule 23 conditional certification motions in federal court; 4) expansive discovery permitted in PAGA litigation; and 5) the reluctance to file cases in federal court wherein PAGA cases cannot be removed.

These claims create potential seven figure exposure for any company with California employees. All industries have been subject to PAGA litigation with business organizations in California now suing the state of California alleging that PAGA is unconstitutional. Attempts to curb abuse of the statute, through legislation, have been generally unsuccessful.

Penalties under PAGA are assessed against employers in the amount of \$100 per employee per pay period for an initial Labor Code violation, and \$200 per employee per pay period for each subsequent violation. (Cal. Labor Code § 2699(f)(2).) These penalties can be collected for each employee for each pay period the employee worked within the statutory period and can add up quickly. Important cases in the appellate court system are currently looking at two key legal issues: 1) can an aggrieved employee obtain multiple penalties per pay period (e.g. if seven penalties in a pay period occur, can the employee recover \$700 or is he/she entitled to \$100); and 2) can an aggrieved employee recover for any California Labor Code violation in a pay period for any aggrieved employee provided that the

employee has suffered at least one, even if it is different than what others have suffered.

There are three categories for which a PAGA claim can be asserted: (1) violations of provisions specifically enumerated under Labor Code § 2699.5; (2) Health and Safety Violations; and (3) all other Labor Code provisions not included above.

### **What Is A PAGA Claim?**

Dubbed the “bounty hunter law,” PAGA, or the Labor Code Private Attorneys General Act of 2004, is actually a series of statutes codified in Sections 2698 through 2699.6 of the California Labor Code that “authorizes aggrieved employees to file lawsuits to recover civil penalties on behalf of themselves, other employees, and the State of California for Labor Code violations.” The employee suing under PAGA acts “as the proxy or agent” of California’s labor law enforcement agency, the LWDA, in policing Labor Code violations. On simpler terms, PAGA confers a private right of action to individuals to prosecute Labor Code violations. PAGA incentivizes this type of lawsuit by authorizing the aggrieved employee to keep 25 percent of any civil penalties collected, while 75 percent goes to the state (Cal. Lab. Code § 2699(f)). In any settlement, counsel obtains approximately 33 percent of the gross settlement as fees prior to this division occurring.

Before filing a PAGA action, the aggrieved employee must exhaust specific administrative requirements by filing a written notice “of the specific provisions of [the Labor Code] alleged to have been violated, including the facts and theories to support the alleged violation,” both online with the LWDA and by certified mail to the employer (Cal. Lab. Code § 2699.3(a)(1)(A)).

Civil penalties under PAGA can be eye-popping. For Labor Code provisions that do not specify the penalty amount, PAGA provides default civil penalties at \$100 for every employee for every pay period for the first violation, and \$200 for each violation thereafter (though case law may provide an argument that PAGA penalties are limited to violations that occur after the PAGA notice). Because separate penalties may be assessed for each Labor Code violation in the same pay period for the same underlying violation, the PAGA penalty exposure for the client can grow exponentially.

## Important PAGA Cases In 2019

*ZB, N.A. v. Superior Court* (2019) 8 Cal 5th. 175 (“Lawson”)

In *Lawson*, the plaintiff filed a PAGA action against her employer sought, among other things, civil penalties and underpaid wages under California Labor Section 558 (“Section 558”). To date, Section 558 was utilized by plaintiffs’ counsel to increase settlement value and potential liability in PAGA cases. Section 558 enables the Labor Commissioner to collect \$50 and \$100 in civil penalties against employers that unlawfully deny overtime compensation and also to recover “an amount sufficient to recover underpaid wages.” Though PAGA provides that amounts recovered by a private litigant are to be distributed 75% to the state and 25% to “aggrieved employees,” section 558 provides that any wage-based recovery under section 558 goes entirely (100%) to the workers. Section 558 was used by plaintiffs’ counsel to pursue a “class action lite” claim by arguing that the wages were recover as a penalty under Section 558, for the year covered under the statute, regardless of the existence of a pre-dispute arbitration agreement.

The Court of Appeal denied ZB's motion to compel arbitration, finding that "underpaid wages" under Section 558 are part of an "indivisible civil penalty," i.e., part of a typical PAGA claim, that cannot be compelled to arbitration. The California Supreme Court agreed with the Court of Appeal that arbitration of a Section 558 claim is not permissible, but for a surprisingly different reason: employees are not entitled to seek "underpaid wages" at all under Section 558, even through PAGA, meaning there is no "victim-specific" claim to compel to arbitration. In short, the California Supreme Court's ruling bars the recovery of underpaid wages, under Section 558, in PAGA litigation.

*Bernstein v. Virgin America, Inc.* (2019) 365 F.Supp.3d 980

In *Bernstein v. Virgin America, Inc.*, the Northern District Court of California ordered Virgin America to pay more than \$77,000,000 in damages, restitution, interest and penalties for a variety of violations of the California Labor Code. The Court awarded the plaintiffs \$45,337,305.29 in damages and restitution as a result of Virgin America’s unpaid wage, overtime and meal and rest period violations. It also imposed wage statement and waiting time penalties in the amount of \$6,704,810. The Court awarded the class \$3,552.71 per day in interest, assessed since October 25, 2018. And the Court imposed \$24,981,150 in civil penalties under PAGA – an amount that reflected a 25%

reduction from the maximum available. In total, the penalties imposed against Virgin America made up more than 40% of the amount awarded to the employees. The matter is currently on appeal to the 9th Circuit. The Bernstein case is one of the few trial court decisions that give guidance on reduction of PAGA penalties and a trial court's consideration regarding same. There are only approximately 25 decisions, since PAGA's inception, where a court has analyzed PAGA penalties and given guidance on its consideration of same.

Magadia v. Wal-Mart Associates, Inc. (2019) 384 F. Supp.3d 1058

Roderick Magadia filed suit against Walmart, alleging the company failed to pay adequate compensation for missed meal breaks and provide adequate wage statements. He also sought penalties under the Private Attorneys General Act (PAGA) for the same violations. In January 2017, Judge Lucy Koh of the U.S. District Court for the Northern District of California certified three classes of employees in the case. Following the granting of summary judgment on some of the claims, the matter proceeded to trial predominantly on damages related issues. Despite decertifying parts of the class, Judge Koh issued a ruling that awarded \$102 million to the certified class and aggrieved employees. Important regarding PAGA is that the damages model offered by Plaintiffs was for \$160 million, but it was reduced to \$54 million by the court. This approximately 67% reduction in the penalties has been cited by employers as a proper calculation of potential risk (i.e. that a reasonable amount may only be \$33 per pay period). This case is also currently on appeal to the 9th Circuit.

Ferra v. Loews Hollywood Hotel, LLC (2019) 40 Cal.App.5th 1239

In another case from the past year, the California Court of Appeal separately considered how to calculate the hour of premium pay owed when employers fail to provide a compliant meal or rest period. The plaintiff in Ferra v. Loews Hollywood Hotel, LLC argued that the meal and rest period premiums were paid improperly because the rate of premium pay was at the employee's base rate (hourly wage) and did not take into account non-discretionary bonuses or similar compensation. The plaintiff further contended that the phrase "regular rate of compensation" should be calculated the same as the "regular rate of pay" used for calculating overtime compensation. Ultimately, the appellate court held that you are obligated to provide a full extra hour of pay only at the employee's base hourly rate. It concluded that you are not required to include additional types of compensation in the calculation. This case is currently on appeal to the California Supreme Court.

## **What Should You Do After Receiving A PAGA Notice? A 10-Step Guide**

Here is a 10-step process you can take after receiving a PAGA notice to ensure your organization is as well-positioned as possible to minimize or avoid liability.

### **1. Contact Labor And Employment Counsel**

A PAGA notice should immediately prompt you to contact your labor and employment counsel, experienced in handling PAGA actions. There are time limits to cure discreet Labor Code violations, more fully discussed below.

### **2. Audit Wage Statements and Payroll Records**

You should review wage statements going back one year from the date of the PAGA notice for compliance with the requirements under Labor Code section 226(a), ensuring they provide: gross wages earned; total hours worked; the number of piece-rate units earned and the applicable piece rate if the employee is paid on a piece-rate basis; all deductions; net wages earned; start and end dates of the pay period; the name of the employee and the last four digits of their social security number or an employee ID number; the name and address of the employing legal entity; and all applicable hourly rates and the corresponding hours worked at each hourly rate. It is worth noting that the time period for which penalties can be assessed is limited to one year before the date of filing of the PAGA lawsuit, not the date of the PAGA notice.

You should also review payroll records to determine to what extent the records are facially non-compliant. Specifically, you should analyze the frequency of meal period entries that show a potential late, short or missed meal that may be inconsistent with California law. This rate should be balanced with the amount of meal period premiums paid. Facially non-compliant rates above 10% should result in much deeper analysis to determine potential non-compliance.

### **3. Make Necessary Corrections**

If you identify problems, you should immediately correct any missing or inaccurate information on the wage statements. Because Labor Code section 226 violations carry the heaviest penalty

amount at \$250 for the initial violation and \$1,000 for subsequent violations, correcting the wage statements soon after the PAGA notice will allow you to argue that there are only a few subsequent violations for which penalties may be assessed, if at all.

As to time records, you should determine whether immediate changes need to be made including, but not limited to, revisions of policy, scheduling of meal and rest periods, location of timekeeping stations and training of supervisions on same.

#### **4. Determine If A “Cure” Is Warranted**

The Labor Code allows you to “cure” two types of wage statement violations: (1) failure to include either the start or end date of the pay period (Cal. Lab. Code § 226(a)(6)); and (2) failure to provide the name and address of the employing legal entity (§ 226(a)(8)). Where such requisite information is missing from the wage statements, you should strongly consider undertaking the cure option, as there are few viable defenses to such violations. Where such requisite information is inaccurate on the wage statements, you should weigh the cost and benefit of the cure option with your counsel. For example, use of an employer’s unexpired fictitious business name that is properly recorded in California has recently been validated.

Undertaking the cure option is no small feat. Specifically, corrected and “fully compliant” wage statements must be provided to every employee for every pay period going back three years from the date of the PAGA notice (Cal. Lab. Code § 2699(d)). The requirement for “fully compliant” corrected wage statements should be interpreted to mean wage statements that comply with all nine requirements set forth in Labor Code section 226(a). You must also file a notice of the cure that includes a “description of actions taken” with the LWDA (§ 2699.3(c)(2)(A)). You have 33 days from the postmark date of the notice to complete the cure. If the wage statement violations have been cured, the law bars the employee from bringing a civil action pursuant to Section 2699 against you.

## **5. Audit Timekeeping And Payroll Records And Practices**

You should also audit your time and wage records to flag potentially troublesome practices, including:

- Do you use a rounding policy?
- Do you automatically deduct time for a meal period?
- Have you ever paid a meal or rest period premium?
- Are employees allowed to leave the premises during meal and rest breaks?
- Are employees paid at their regular rate of pay for overtime?
- Have you strictly complied with requirements if adopting an alternative workweek schedule?
- Do you maintain or cover the cost of maintaining uniforms?

This is not an exhaustive list of the potential wage and hour violations, but you and your counsel should audit your records and identify practices and policies that may give rise to Labor Code violations.

## **6. Determine If The Employee Is Aggrieved**

An employee may seek civil penalties under PAGA on behalf of themselves and other current or former employees so long as they have suffered at least one alleged Labor Code violation. Although this appears to be a low threshold, the applicable statute of limitations as to each claim should be analyzed by counsel. For example, an employee who went on disability leave more than a year before the date of the PAGA lawsuit would not have worked within the past year that would serve as the basis for any meal and rest violations.

## **7. File A Brief Employer's Response With The LWDA, If Desired**

Although you are not required to file a response addressing the charges in the PAGA notice, standard practice for many counsel is to file a written response with the LWDA. The response should be kept brief without going into any details about any expired statute of limitations or how the alleged facts and theories are deficient. It is sufficient to say that the PAGA notice fails to identify sufficient facts to allow either LWDA or you to conduct an investigation.

## **8. Gather Counterintelligence**

Because PAGA actions are generally a product of a copious amount of information that has been amassed by the employee's counsel prior to providing the PAGA notice, you should also use counterinvestigative strategies, such as encouraging employees to report any outside contact inquiring about working conditions, or wage and hour matters. Your investigation should include review of the employee's social media accounts, as well as a comprehensive search of social media for advertising referencing the employee or your organization. This is particularly essential for companies with large workforces, as social media advertisements carry the potential to reach the widest audience.

## **9. Review The Employee' Personnel File**

Your call to action is often triggered before you even receive a PAGA notice. In most cases, the employee's counsel will send you a request for the employee's personnel file long before any notice is filed with the LWDA. You should consult a seasoned labor and employment counsel to flag potential wage and hour violations and develop a game plan prior to receiving the inevitable PAGA notice.

## **10. Assess Early Settlement**

Settlement trends in 2018 for combined class and PAGA actions show that the cost of buying peace increases as the case progresses. A PAGA-only action without class action component will often be turned into a hybrid class/PAGA action for settlement purposes. Indeed, it makes most sense for employers to obtain the broadest release possible, since the PAGA claims will be based on wage and hour violations that trigger class damages separate from PAGA penalties.

The average amount of settlements tends to hold steady until 2.5 years after commencement of the lawsuit, after which point the average cost of settlement quickly escalates. This trend reflects the realities of litigation, in that the parties, after 2.5 years of formal litigation, are likely to have invested significant time and money into the case, and are thereby less willing to compromise their position for settlement. Depending on the type and extent of the wage and hour violations, some

claims should be litigated, while others are better left tabled. An experienced PAGA practitioner should be able to chart the best course of action and guide you through the legal terrain.