Insights, News & Events

SO WHAT DO WE DO ABOUT PAGA? THE CONTINUED VIABILITY OF SEVERANCE AGREEMENTS IN THE WAKE OF KIM V. REINS

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Service Focus

California Class Actions and PAGA

Wage and Hour

For decades, severance agreements have been a staple of the employment relationship, inhering to the benefit of employers and employees alike. Through their use, employers are able to obtain peace of mind against future litigation while simultaneously providing employees with the added comfort and security of a parting lump-sum payment.

Recently, however, the California Supreme Court's March 2020 decision in *Kim v. Reins* has called into question the continued viability of these agreements by holding that an employee's injury has no bearing on their ability to sue under the Private Attorneys General Act (PAGA). As a result, using severance agreements to settle any potential Labor Code violations that might have occurred during the employment relationship no longer provides the same protection against future suits, especially PAGA actions. For that reason, it is important to understand the logic underlying *Kim v. Reins*, the decision's impact on severance agreements, and what options you still have moving forward.

Kim v. Reins And The Inescapable PAGA Claims

At its core, *Kim v. Reins* is a case about the California Labor Code Private Attorneys General Act of 2004, or PAGA —a statute that allows an allegedly "aggrieved

employee" to sue an employer for alleged Labor Code violations, on behalf of themselves and other "aggrieved employees." In a PAGA case, the employee acts not in their individual capacity, but as a representative of the government, and seeks to collect civil penalties on behalf of the state, rather than wages, interest, and statutory penalties payable to employees directly.

PAGA provides that in any judgment, "aggrieved employees" keep 25% of whatever the representative plaintiff collects, relinquishing the remaining 75% to the state's coffers. Because of this, in practice, employees usually bring PAGA claims (i.e. seeking civil penalties) in tandem with other claims (i.e. seeking unpaid wages, interest, and statutory penalties) to maximize their potential recovery on each alleged Labor Code violation.

Enter *Kim v. Reins*. There, the employer faced the classic example of a hybrid class action/ PAGA claim alleging a slew of alleged Labor Code violations. Based on an arbitration agreement, the named representative's individual claims were submitted to arbitration, and the class claims were dismissed. While the case was in individual arbitration, the employer and the named representative settled the named representative's individual claims (not via a traditional settlement and release, but via a formal procedure called an "offer of judgment"). Based on such settlement, the employer then moved to dismiss the related PAGA claims.

According to the employer, compensating the plaintiff for his alleged injuries in an agreed-upon amount meant that he was no longer an "aggrieved employee" with the requisite jurisdictional standing (i.e. the right to sue) under PAGA. Unfortunately, the California Supreme Court rejected this argument in a March 2020 decision by maintaining that an employee's continued injury, or lack thereof, has no bearing on their standing or ability to bring suit under PAGA — apparently, or potentially, under a principle of "once aggrieved, always aggrieved."

RESULTING CONCERNS FOR SEVERANCE AGREEMENTS

In the wake of this decision, some attorneys are concerned that the ability of employers to use individual settlements and releases to insulate themselves against future PAGA claims may be in doubt. The concern is that, under the state Supreme Court's reasoning that the ability of a PAGA representative to act as such does not depend on the continued viability of their individual claims, commonly used severance and release agreements may no longer act as a bar to future suits under the PAGA framework.

Importantly, however, *Kim v. Reins* did not involve a severance agreement, nor did it involve a similarly common pre-litigation settlement in response to a demand letter. Although it is unclear how the case would have applied in these scenarios (as it arose from a unique procedural history involving an individual arbitration and offer of judgment), many employment attorneys have flagged this as a potential issue in future cases.

POTENTIAL ALTERNATIVE OPTIONS MOVING FORWARD

Luckily, employers still have a few potential methods to deal with the threat of PAGA suits when crafting severance agreements. This is because *Kim v. Reins* ties its holding to the issue of standing – or, in other words, whether a right to sue under PAGA exists. Even if that right to sue exists, however, an employee may still be able to give up that right through a valid waiver or release agreement. Or even if an employee lacks the ability to give up that right, the employee could simply agree not to take steps to enforce it through a "covenant not to sue." In each case, however, different considerations or limitations apply.

WAIVERS/RELEASES

In short, a waiver or release is generally regarded a voluntary relinquishment of a known right. In *Iskanian v. CLS Transport,* the California Supreme Court

suggested that employees could readily waive their right to sue as a PAGA representative so long as a dispute had already arisen of which the employee was aware. In essence, it creates a work-around for the holding in *Kim v. Reins*. Specifically, the Supreme Court noted in *Iskanian v. CLS Transport*:

Of course, employees are free to choose whether or not to bring PAGA actions when they are aware of Labor Code violations. But it is contrary to public policy for an employment agreement to eliminate this choice altogether by requiring employees to waive the right to bring a PAGA action before any dispute arises.

In *Julien v. Glenair,* a California Court of Appeal then clarified that, for this type of PAGA waiver, this pre-dispute/post-dispute boundary is crossed after the employee notifies the LWDA of the alleged violation and the time for the LWDA to take the case itself as a government enforcement agency has expired. With the LWDA having relinquished its right to proceed, only then does the employee become a formal representative of the state under PAGA, with the ability to waive, or give up, their state right to serve as a PAGA representative.

Accordingly, if an employee has already gone through the LWDA notification process by the time severance is offered, the employee would have full authority to enter into an enforceable PAGA waiver contained in a severance agreement.

COVENANTS NOT TO SUE

By contrast, Matthew Bender's Practice Guide notes that unlike a waiver, "a covenant not to sue is not a present abandonment or relinquishment of a right or claim, but merely an agreement not to enforce an existing cause of action." This is a distinction with a difference. In other words, claims are not being released or deemed not to have merit; the plaintiff is simply agreeing not to go to court to enforce them.

Theoretically, an employee could therefore agree not to bring suit under PAGA, without having to actually give up the state-controlled right to serve as a representative. Because no state-controlled right is being relinquished in a covenant not to sue, there would be no reason to wait for the completion of the LWDA notification process. Rather, *Iskanian v. CLS Transport* suggests that a covenant not to sue under PAGA could be enforceable as soon as the employee becomes "aware" of the potentially alleged Labor Code violations, or at least aware of the facts and circumstances (such as the amount of wages paid to him or her) from which such claims may allegedly arise.

Accordingly, if an employer has taken active steps to notify an employee of their rights, or the employee is aware of potential Labor Code violations by the time severance is offered, an employee may have a difficult time arguing that a covenant not to sue should not be enforced. Based on certain constructive knowledge doctrines, an argument could even be made that a covenant not to sue an employer in court is enforceable *regardless* of whether an employee was aware of any violations, so long as the employee *should have been* aware based on their personal experiences or received documentation (such as through regularly received paystubs outlining their pay calculations). This is especially true if the employee was paid out of a settlement agreement as an incentive not to bring claims *of any kind* in court.

A WORD ABOUT CALIFORNIA CIVIL CODE § 1542

In both of the above cases, it also bears noting that a California Civil Code section 1542 waiver could fundamentally change the analysis. These waivers are a staple of both severance and settlement agreements in California. In essence, they are designed to allow employees to waive an employer's liability for claims that the employees are *unaware* of at the time of the agreement's execution. As neither *Kim v. Reins*, *Iskanian v. CLS Transport*, nor *Julien v. Glenair* dealt with this specific type of statutory waiver, the effect of

these waivers on an employee's right to serve as a PAGA representative remains to be seen.

CONCLUSION

Ultimately, no solution is foolproof when using severance agreements to mitigate the risk of prospective PAGA litigation. While theoretically sound, the issue of how to handle PAGA waivers, covenants not to sue, 1542 waivers, or other severance devices, is still very much an open legal question subject to judicial determination and reasonable dispute. What resonates with one judge may miss the mark with another.

Although caution is recommended, fully informed employers may well be able to successfully circumvent the impact of *Kim v. Reins* and repeated exposure to PAGA actions which have become all too common in the present litigation environment. Importantly, prior to implementing any of the above strategies in your own workplace, it is critical to consult with your local labor and employment attorney to determine the best course of action based on your company's own unique goals and objectives, including tolerance for risk in this developing area of the law.