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INSIDE THIS ISSUE:

Employer Punished For Enforcing Employee Non-Compete Agreement

By Christopher W. Olmsted

After a business bestows an employee with training and inside information regarding company operations or customers, it has an earnest purpose in seeking to restrain that employee from working for a competitor. But in California, non-competition agreements are generally not enforceable in court.

Fine, you say, I won't go to court. But if I know that an applicant or employee has signed such an agreement, I'll refuse to hire or employer that employee because I want to adhere to an "industry code of honor." Do unto others as I would have them do unto me. No problem, right?

Not so fast. A competitor was sued after firing an employee after learning that she had signed a non-competition agreement with her prior employer. In a case titled *Silguero v. Floor Seal Technology, Inc.*, the company received some bad news from a California appellate court.

An Employee Promises Not To Compete

In 2003, Rosemary Silguero began employment with Floor Seal Technology, Inc. as an in-house sales representative where she placed telephone orders for the company's products. Five years into her employ

(Continued on page 2)

Non-Compete Agreements Are Generally Not Enforceable In California, With Only Very Narrow Exceptions

(Continued from page 1)

ment, the company forced Ms. Silguero to sign an agreement which prohibited her "from all sales activities for 18 months following either departure or termination." About two months after Ms. Silguero signed this non-competition agreement, the company terminated her employment.

Employee Hired By Competitor

After the termination, Ms. Silguero soon found employment with a competitor, Creteguard, Inc. Floor Seal Technology contacted Creteguard and requested the cooperation and participation of Creteguard in enforcing the employee agreement, including those provisions prohibiting Ms. Silguero from all sales activities for 18 months following Silguero's departure or termination from Floor Seal Technology.

New Employer Fires Employee

In response, Creteguard's chief executive officer informed Ms. Silguero in writing that "it has been brought to my attention . . . that you have signed a confidentiality/non-compete agreement with your past employer. We regret to inform you that Creteguard is unable to continue your employment effective today. Although we believe that non-compete clauses are not legally enforceable here in California, Creteguard would like to keep the same respect and understanding with colleagues in the same industry."

Unemployed Again, Off To Court

Out of a job for the second time, Ms. Silguero sued Cretegaurd for wrongful termination. She alleged that the Floor Seal Technology noncompetition agreement honored and enforced by Creteguard was void pursuant to California Business & Professions Code section 16600, and that Creteguard's "enforcement and ratification of an illegal and void non-compete agreement . . . violated . . . the public policy of the State of California."

Creteguard filed a motion seeking dismissal of the case. The trial court granted the motion in favor of Creteguard. However, Silguero appealed from the judgment.

California Law Voides Employee Non-Competition Agreements

California law renders employee non-competition agreements unenforceable. California Business and Professions Code Section 16600 provides: "Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."

There are only four exceptions to this rule:

- The purchaser of a business may restrict a seller from engaging in subsequent competition which would reduce the value of the property right acquired;
- Partners may restrict a withdrawing partner from engaging in competition where there is a risk that a partnership's goodwill would be diminished;
- Dissolving limited liability companies may restrict a partner from carrying on a similar business within a specified geographic area; and
- An employer may use a covenant to protect the employer's trade secrets.

Tameny Claims

Generally, an employee who is terminated in violation of an important public policy may assert a wrongful termination claim, also known as a "Tameny claim" in honor of a 1980 case titled *Tameny v. Atlantic Richfield Co.* In the Tameny case as well as

(Continued on page 3)

(Continued from page 2)
subsequent cases, the California Supreme Court recognized that "although employers have the power to terminate employees at will, they may not terminate an employee for a reason that is contrary to public policy."

In the present case, the appellate court determined that terminating an employee on account of a non-competition agreement, a contract which in itself is contrary to public policy, gives rise to a Tameny claim for wrongful termination.

The court noted that the California law voiding non-competition agreements has been around for over 100 years, and "our courts have consistently affirmed that Business & Professions Code section 16600 evinces a settled legislative policy in favor of open competition and employee mobility." This is a strong public policy protecting every employee. "The law protects Californians and ensures that every citizen shall retain the right to pursue any lawful employment and enterprise of their choice," noted the court.

Liability For Honoring Another Company's Non-Compete

Turning to Ms. Silguero's misfortune, the court determined that she did have legal recourse against her second employer who decided to fire her in order to honor her former employer's non-compete agreement.

The court observed that Creteguard (the second employer) admitted that it entered into an understanding with Floor Seal (the original employer) to honor Floor Seal's noncompetition agreement. Creteguard did this despite knowing that that non-compete clauses are not legally enforceable here in California.

The court reasoned: "this understanding is tantamount to a no-hire agreement." Such "understanding"" between Creteguard and Floor Seal would be void and unenforceable under section 16600 because it unfairly limits the mobility of an employee and because Floor Seal "should not be allowed to accomplish by indirection that which it cannot accomplish directly."

The appellate court concluded that the trial court erroneously dismissed Ms. Silguero's Tameny claim (wrongful termination claim) against Creteguard. The case was reinstated and sent back to the trial court for further proceedings.

Practical Points:

No Non-Competes. Since such agreements are not enforceable, it is best not to ask employees to sign them.

Don't Honor Non-Competes. Don't repeat the mistake made by the second employer in this case. Employment decisions should not be based on non-compete agreements.

Exceptions Are Narrow. Realize that there are only four exceptions to the ban on non-competes (see above), and those do not usually apply to the typical employee.

Attack the problem other ways. Businesses are validly concerned about maintaining confidential and trade secret information. Agreements forbidding the use of such proprietary information, if carefully worded, are enforceable.

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Agreements forbidding the use of such proprietary information, if carefully worded, are enforceable.

Workers Deemed Independent Contractors With No Right To Sue For Discrimination

Courts are more willing to deem workers independent in certain occupations, and not so in others.

There have been a lot of cases lately where courts have determined that businesses have misclassified workers as independent contractors rather than employees. Legal liability for such misclassifications can be high. On the other hand, there are many benefits associated with hiring true independent contractors. Legally, for example, such workers are not "employees" and therefore they have no standing to sue for employment discrimination. In a recent Ninth Circuit case titled *Murray v. Principal Financial Group, Inc.* an appellate court upheld the dismissal of a Title VII discrimination claim on the ground that the worker was an independent contractor.

Sales Agent Sues for Sex Discrimination

The plaintiff in this case, Patricia Murray, is a "career agent" for the defendants, Principal Financial Group, Inc. Murray and other Principal career agents sell Principal products that include a wide range of financial products and services, including annuities, disability income, 401(k) plans, and insurance. Murray sued Principal for sex discrimination in violation of Title VII. The trial court dismissed her claim, finding that she was an independent contractor who had no right to sue under Title VII.

But She Was An Independent Contractor

In her appeal, Murray argued that although Principal called her an independent contractor, she was in reality a regular employee. She contended that the company exercised sufficient control over the conduct of her duties to qualify her as an

employee.

The court of appeal disagreed. It noted that most federal courts have held that insurance agents are independent contractors and not employees for purposes of various federal employment statutes, including the Employee Retirement Income Security Act ("ERISA"), the Age Discrimination in Employment Act ("ADEA"), and Title VII.

Title VII Test For Independent Contractor Status

When determining whether an individual is an independent contractor or an employee for purposes of Title VII, a court should evaluate "the hiring party's right to control the manner and means by which the product is accomplished."

There are a number of factors relevant to this "right to control" inquiry. They include:

[1] the skill required;

[2] the source of the instrumentalities and tools;

[3] the location of the work;

[4] the duration of the relationship between the parties;

[5] whether the hiring party has the right to assign additional projects to the hired party;

[6] the extent of the hired party's discretion over when and how long to work;

[7] the method of payment;

[8] the hired party's role in hiring and paying assistants;

[9] whether the work is part of the regular business of the hiring party; [10] whether the hiring party is in business;

[11] the provision of employee benefits; and

[12] the tax treatment of the hired party.

These factors are quite similar to other independent contractor

(Continued on page 5)

(Continued from page 4)
tests, such as California's common law *Borrello* test applicable in the workers' compensation context.

Murray Is Independent

Reviewing the evidence, the court confirmed that Ms. Murray was an independent contractor, not entitled to sue for sex discrimination.

Murray is free to operate her sales agent business as she sees fit without day-to-day intrusions."

Murray decides when and where to work, and in fact maintains her own office, where she pays rent.

She schedules her own time off, and is not entitled to vacation or sick days.

Murray is paid on commission only, reports herself as self-employed to the IRS, and sells products other than those offered by Principal in limited circumstances.

OK That A Few Factors Are Absent

The court acknowledged that not all of the independent contractor factors were satisfied; however, the balance weighed in favor of independent status.

The court wrote: "Murray receives some benefits, has a long term relationship with Principal, possesses an at-will contract, and is subject to some minimum standards imposed by the hiring party. These, however, on balance, are insufficient to overcome the strong indications that Murray is an independent contractor."

The court continued: "The parties dispute the minutiae of some aspects of Murray's relationship with Principal, relating to who bears responsibility for providing some of the instrumentalities and tools required for Murray to perform her job, the degree of autonomy that Murray has to select and retain her assistant, and the degree to which Principal requires Murray to document and report her work. Even when all of these issues are resolved in Murray's favor, however, the overall picture presented by Murray's relationship with Principal is still one of an independent contractor rather than an employee. The defendants do not control the manner and means by which Murray sells their financial products."

Accordingly, the appellate court upheld the trial court's decision to dismiss the claim.

Practical Tips:

Properly Classify. Although in this case the court agreed that the worker was an independent contractor, the test is inexact and you should carefully scrutinize the factors before making a decision. It is prudent to seek legal advice.

Occupations Matter – Kind Of. Courts are more willing to deem workers independent in certain occupations, and not so in others. For example, last month's Legal Update included an article on delivery drivers who were improperly classified. There have been a number of adverse decisions relating to drivers.

The Applicable Law Matters. There are a number of different tests which apply to independent contractor status. The EEOC has one for discrimination claims, the IRS has one for tax purposes, the workers' compensation system and the labor agencies have their own tests as well. Many of the factors are similar but there are some differences. It is of course important to comply with all of the tests.

Free Chart. Our complimentary concise information sheet, "Determining Independent Contractor Status" will help educate you. It is available upon request. I will send you the free document if you contact me at cwo@barkerolmsted.com.

There are several different independent contractor tests, depending on the enforcing agency and applicable law.

California Supreme Court Makes Employer Summary Judgment Motions More Improbable

Employers face a difficult challenge when attempting to end a case by summary judgment...and the California Supreme Court just made it more difficult.

When an employee sues his employer alleging discrimination, he often lacks direct evidence that the decision maker acted on an illegal motive. The evidence is often circumstantial. Sometimes, among other evidence, employees seek to establish discriminatory decision by offering evidence that a co-worker or other uninvolved employee made a "stray" derogatory remark. Should that evidence be admissible? Under federal law, the evidence is often excluded, but in California the admissibility of such stray remarks has been up in the air—until the recent California Supreme Court case *Reid v. Google*.

Why Is It Important?

Before a trial takes place, an employer may file a motion for summary judgment. The motion asks the court to enter judgment in favor of the employer without the need for a trial. Essentially the motion argues that trial is unnecessary because the employee is unable to produce sufficient evidence to win at trial.

Employees attempt to defeat such motions by introducing all sorts of circumstantial evidence that an adverse employment decision was motivated by discrimination, including off-hand derogatory "stray remarks" made by co-workers and other non-decision makers. The California Supreme Court's ruling addresses whether such stray remarks may be considered.

Employee Sues Google For Age Discrimination

Google hired Brian Reid as a director of engineering at the age of 52. In his first year he received a good performance review, but he was told he didn't quite fit in.

His manager wrote: "Adapting to Google culture is the primary task for the first year here. Right or wrong, Google is simply different: Younger contributors, inexperienced first line managers, and the super fast pace are just a few examples of the environment."

Another manager described his opinions and ideas as "obsolete and "too old to matter," adding that he was "slow, fuzzy, sluggish, and lethargic," and that he did not "display a sense of urgency" and "lacked energy." Other coworkers called Reid an "old man, "an old guy," and an "old fuddy-duddy," told him his knowledge was ancient."

Reid was later shuffled out of his director position and eventually laid off. He sued Google, alleging age discrimination under the California Fair Employment and Housing Act (FEHA).

Federal Stray Remarks Doctrine

Leading up to the California Supreme Court's decision, legal commentators had wondered whether California will follow the federal rule. Under federal case law, stray remarks are often excluded from evidence. The term "stray remarks" first appeared in a 1989 concurring opinion by Justice O'Connor in *Price Waterhouse v. Hopkins*.

In that case, the plaintiff, a senior manager at a nationwide professional accounting firm, sued her employer for sex discrimination when it refused to re-propose her for partnership. Justice O'Connor stated that "stray remarks" – "statements by non-decisionmakers, or statements by decisionmakers unrelated to the decisional process itself" -- do not constitute direct evidence of decision makers' "substantial negative reliance on an illegitimate criterion in reaching their decision."

However, Justice

(Continued on page 7)

(Continued from page 6)
O'Connor explained that stray remarks can be probative of discrimination, and ultimately concluded that the plaintiff provided the requisite direct evidence that decision makers had unlawfully based their decision on gender. Such evidence included remarks by a partner suggesting she should "walk more femininely, talk more femininely, dress more femininely, wear make-up, have her hair styled, and wear jewelry" to improve her chances for partnership, and comments by other partners describing the plaintiff as "macho" and advising her to take "a course at charm school."

Federal courts have widely adopted this stray remarks doctrine. Under this doctrine, federal circuit courts deem irrelevant any remarks made by non-decisionmaking coworkers or remarks made by decisionmaking supervisors outside of the decisional process. Courts will grant an employer's motion for summary judgment where the employee's evidence is based only on such stray remarks.

For example, in one case a coworker's comments that plaintiff was a "useless old lady" who needed to retire, was a "troubled old lady," and was a "damn woman" did not influence the decisional process and, therefore, were not relevant. In another case, a direct supervisor's statements that plaintiff was an "old fart" and that a younger person could do faster work deemed "a mere stray remark . . . insufficient to establish age discrimination."

Sometimes stray remarks are deemed stray remarks because they too ambiguous to attribute to discriminatory motive. For example, in one case a supervisor's comments that she wanted "new blood," a "quick study," and someone with "a lot of energy" did not reflect age bias.

California Rule: Stray Remarks Are Relevant

In California, some appellate courts have followed the stray remarks doctrine, while others have rejected it. The California Supreme Court took up the *Reid* case to create a clear rule.

Google of course wanted the Court to adopt the stray remarks doctrine. Google argued that the rule should be adopted in California so that courts can "disregard discriminatory comments by co-workers and nondecisionmakers, or comments unrelated to the employment decision" "to ensure that unmeritorious cases principally supported by such remarks are disposed of before trial." It argued that application of the stray remarks doctrine is an important means for trial courts to sift out cases "too weak to raise a rational inference that discrimination occurred."

On the other hand, Reid argued that courts should not view the remarks in isolation, but that those remarks should be considered with all the evidence in the record.

The California Supreme Court sided with Reid, ruling that such remarks can be considered along with other evidence.

Supreme Court Rationale

The Court gave several reasons for its rejection of the stray remarks doctrine. First, strict application of the stray remarks doctrine would result in a court's categorical exclusion of evidence even if the evidence was relevant. An age-based remark not made directly in the context of an employment decision or uttered by a non-decision-maker may be relevant, circumstantial evidence of discrimination. It could reflect the decisionmaker's motive or it could have influenced the adverse decision.

Second, a categorical rejection of such evidence would be contrary to the state's summary judgment rules. Those rules require a court to consider all evidence offered and all inferences which may be drawn from the evidence.

Third, the stray remarks are part of the whole picture. It is a "common-sense proposition" that a slur, in and of

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Stray remarks made by co-workers or non-supervisors may be relevant in showing discriminatory personnel decisions.

Appellate Court Reinstates Disability Claim By Employee Disabled By Stroke

What happens when a company terminates a poor-performing employee who has recently suffered a stroke? It depends. Can the company demonstrate objectively poor performance, or are the reasons subject to debate? Has management made questionable comments regarding the disability, or focused only on legitimate business concerns? The wrong answers lead to litigation, as an employer recently discovered in a California case titled *Sandell v. Tylor-Listug, Inc.*

Performance Problems After A Stroke

Terry Sandell worked as the vice president of sales at Taylor-Listug, a guitar manufacturer. About six months into his employment, he suffered a stroke and did not return to work until several months later.

When Sandell returned to work, he required a cane to walk because he had difficulty with his balance and strength. His speech was noticeably slower than it had been prior to his stroke.

Sandell claimed that not long after he returned to work, his manager came in his office, closed the door and said that if he didn't make a full recovery, that the company had the right to fire him

(Continued on page 9)

Employees terminated for poor performance might point to good performance reviews to show the reason is false.

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itself, does not prove actionable discrimination. A stray remark alone may not create a triable issue of age discrimination. But when combined with other evidence of pretext, an otherwise stray remark may "create an ensemble that is sufficient to defeat summary judgment."

Fourth, the rule is too difficult to apply. The rule suggests that remarks by non-decisionmakers are not considered, yet it is often difficult to determine who was involved in the decisionmaking process, and who may have been an influencer. Moreover, the federal courts have been inconsistent in what is considered to be related to discriminatory motive. For example, some federal courts have found employers' statements about the need for "new blood" or "young blood" to be ageist remarks, while others have not.

Accordingly, the California Supreme Court rejected the "stray remarks doctrine," ruling that evidence of such remarks may be considered by courts ruling on motion for summary judgment motions.

Comments:

It has always been challenging for an employer to win a motion for summary judgment in an employment discrimination case, and the California Supreme Court has just made it even more difficult.

A company is made up of all sorts of individuals, most of whom do not speak or act on behalf of the company when it comes to personnel decisions. The Court's decision makes any remark made by every insensitive boor the potential grist for the litigation mill. Oftentimes management or HR will not know that such comments were made until a lawsuit is filed and the plaintiff's deposition has been taken. By then it is too late to take any corrective action.

Nevertheless, businesses must remain as diligent as ever when it comes to disapproving of inappropriate remarks which may reflect on an employee's protected classification (age, race, gender, religion, etc.) Employees should be disciplined for making such remarks, or even joking about it. Of course a workplace free of any such remarks is a good thing even absent the threat of litigation.

(Continued from page 8)
or demote him and reduce his salary.

Sandell also said that on another occasion, the manager questioned Sandell's use of a cane, suggesting that Sandell was using the cane to create sympathy or to get attention

The manager also criticized his work performance. He told Sandell that he wanted Sandell to "be more of a cheerleader type of personality in the sales department."

Guitar sales fell during this period and the parties disagreed as to the cause; it was perhaps the economy, or pre-existing problems in the department, but also perhaps Sandell's leadership in the sales department.

Sandell of course claimed that he did a good job. He also pointed to favorable performance reviews.

Sandell's written evaluation for 2004 (the year he had the stroke) indicated that Sandell was meeting or exceeding requirements in all of the areas in which he was reviewed, with the exception of one area entitled "Results." In that area, his manager noted "Must Improve." However, in his comments under this section, the manager indicated that he felt he "[had] to say that" because sales had declined that year, for the first time in 20 years. The compamy also took some of the blame for the poor sales by noting that Sandell had come into a sales department that was "in some turmoil" after the departure of the previous vice-president of sales. The manager indicated in his comments that Sandell had already introduced helpful new approaches for the sales department.

In 2005 Sandell's review was favorable, except that the manager wanted to see "more enthusiasm," and for him to be more "outgoing and friendly." The 2006 rating was also favorable, but noted some problems with leadership drive.

Sandell's manager terminated Sandell's employment in late 2007, a few days after Sandell's 60th birthday, citing displeasure with Sandell's performance as vice president of sales.

Sandell sued, alleging disability and age discrimination. The trial court granted the company's motion for summary judgment, but Sandell appealed.

Stroke Caused Disability Under FEHA

The appellate court considered the question of whether Mr. Sandell was "disabled" as defined by the California Fair Employment and Housing Act ("FEHA"). The court found that he was.

The court noted that the California definition of disability is very broad, and courts are to interpret the provisions liberally in order to protect as many disabled workers as possible. Under FEHA, a person is "physically disabled" when he or she has a physiological condition that "limits a major life activity." A qualifying disease or condition "limits a major life activity" if it makes the achievement of the activity "difficult."

Sandell presented evidence that following the stroke, he had difficulty walking and speaking. He used a cane while walking and his speech was slower than before. Walking and speaking are "major life activities." Since these activities became more difficult for Sandell after the stroke, the court determined that he was disabled under FEHA.

Inconsistent Evidence Regarding Poor Performance Creates Circumstantial Evidence Of Discriminatory Motive

Having determined that Mr. Sandell was disabled as defined by the law, the court next addressed the question of whether the company discriminated against him based on his protected status.

First, the court noted that company manage-

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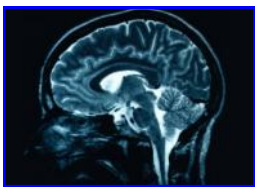

Offhand negative remarks about an employee's protected status might support a discrimination claim.

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ment was aware of Sandell's disability because they noted his slower speech and his use of a cane.

Second, the court concluded that although the company offered legitimate, nondiscriminatory reasons for the termination, Sandell presented evidence calling that evidence into doubt. This was sufficient to send the case to a jury trial.

Taylor-Listug claimed that it terminated Sandell for poor performance. It contended that Sandell did meet sales goals and did not adequately lead and inspire the sales team. It presented a number of complaints from his sales team.

Sandell pointed to his performance reviews, which were overall positive with a "meeting requirements" rating. Although the reviews did include some criticism, he argued that it was not so bad as to justify his termination. He also presented evidence that although sales dropped, they did not decrease as much as the guitar market generally; i.e. he saved the company from much worse declines. Further, he showed that although the some sales team members complained about him once the lawsuit was filed, no such complaints were ever made while he worked for the company.

Negative Comments About Disability Suggests Discriminatory Motives

Sandell also pointed to the comments made by his manager regarding his disability. He referred to the manager's comment that the company had the right to fire him if he did not make a full recovery. He also pointed to the comments about his use of the cane for sympathy. Sandell argued that these comments show that the manager had animosity towards him on account of his disability.

The court found that this evidence was sufficient for a jury to hear. "The evidence is in conflict, and it is not up to the court to weigh conflicting evidence or to assess the credibility of witnesses," wrote the court. "Rather, the court's duty is to determine only whether the evidence could, as a matter of law, support a judgment in favor of the nonmoving party. Here, the evidence is such that a reasonable fact finder could conclude that Taylor-Listug's proffered reasons for terminating Sandell's employment were unworthy of credence, and, based on that conclusion, infer that those reasons are not the real reasons for Taylor-Listug's termination of Sandell."

The appellate court therefore ruled that the trial court had erred by granting judgment in favor of the company. The court reversed this ruling and sent the case back for a jury trial.

Practical Tips:

Performance Reviews Matter. Train managers in the art of performance reviews. Supervisors do a disservice when reviews turn a blind eye to performance deficiencies. Those good reviews cause problems later on when the company must take action against a non-performing employee.

Prefer Objectivity. A person with a disability, including a stroke, must still perform essential job functions, with or without reasonable accommodation. Objective job performance criteria (e.g. measurable results) are preferable because they are less susceptible to implied improper motives than subjective standards (e.g. "attitude" or "enthusiasm").

Avoid Stray Remarks. Train managers to refrain from making offhand remarks about an employee's protected status. Stray remarks referencing a person's disability always come back to haunt.

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