

Application of California Wage Law to Non-residents May Have Even Broader Implications

By Dennis D. Law and Kathryn M. Eppright

Introduction

Like the aftershocks of a California earthquake, the impact of the Ninth Circuit's decision in *Sullivan v. Oracle* ("*Sullivan I*")¹ is being felt across the country. In a class action brought on behalf of Oracle employees who worked periodically in California, the court in *Sullivan II* held that businesses outside of California must abide by California's strict wage and hour laws if any of their employees work within the state for even as little as one day.² Employees who have heretofore been routinely dispatched to California from other states for trade shows, sales calls, and other relatively modest activities will now most likely trigger California's overtime laws, which differ dramatically from federal overtime laws and those of other states. Add in California's rest and meal break requirements, and you have the formula for a lucrative class action, particularly if businesses outside of California fail to take notice of or heed the holding of this significant case.

Facts

Oracle, a Delaware corporation with its principal place of business in California, employs "instructors," who Oracle originally classified as exempt from state and federal overtime laws. Specifically, these employees were categorized by the company as "teachers" exempt from the overtime requirements under California's Labor Code and the federal law, the Fair Labor Standard Act ("FLSA").³

In 2003, instructors employed by Oracle filed a class action in the United States District Court for the Central District of California⁴ alleging that the instructors were misclassified and were not, in fact, exempt from overtime laws. The district court certified two classes: one for employees seeking damages under the California Labor Code and the other for employees seeking damages under the FLSA. At that point, Oracle settled *Sullivan I*.⁵ Although the settlement resulted in the dismissal with prejudice of *Sullivan I*, it specifically excluded any claims of employees "for any periods of time they may have worked within the State of California when they were not a resident of the State."⁶ Accordingly, those claims were dismissed *without* prejudice.⁷

Also in 2003, probably as the result of the filing of *Sullivan I*, Oracle reclassified its instructors working in California and began paying overtime.⁸ In 2004, the company made the same change for the remaining instructors who worked in other states.⁹ Oracle did not, however, pay for any overtime retroactively for work performed before the reclassification.¹⁰

Sullivan II followed shortly after the settlement of *Sullivan I*, filed by three employees of Oracle who worked periodically in California, but were residents of other states.¹¹ Plaintiff Donald Sullivan ("Plaintiff Sullivan") resided in Colorado and worked as an instructor for Oracle from 1998 through 2004, working approximately 74 days in California between 2001 and 2004.¹² Plaintiff Deanna Evich ("Plaintiff Evich") was also a resident of Colorado who worked for Oracle from 1999 to 2004, working a total of approximately 80 days in California between 2001 and 2004.¹³ Plaintiff Richard Burkow ("Plaintiff Burkow") worked for Oracle from 1998 to 2002 while residing in Arizona, and worked approximately 20 days in California between 2001 and 2002.¹⁴

The case was originally filed in California state court, but was removed by Oracle to the federal district court for the Central District of California and was assigned to the same

¹ 2008 U. S. App. LEXIS 23394 (9th Cir. November 6, 2008).

² 2008 U. S. App. LEXIS 23394, at 26–27.

³ 2008 U. S. App. LEXIS 23394, at 4.

⁴ Gabel & Sullivan v. Oracle, Case No. SACV 03-348 AHS (MLGx) (C.D. Cal. Mar. 29, 2005) ("*Sullivan I*").

⁵ *Sullivan II*, 2008 U. S. App. LEXIS 23394, at 6.

⁶ 2008 U. S. App. LEXIS 23394, at 6.

⁷ 2008 U. S. App. LEXIS 23394, at 6.

⁸ 2008 U. S. App. LEXIS 23394, at 5.

⁹ 2008 U. S. App. LEXIS 23394, at 5.

¹⁰ 2008 U. S. App. LEXIS 23394, at 5.

¹¹ 2008 U. S. App. LEXIS 23394, at 3–4.

¹² 2008 U. S. App. LEXIS 23394, at 3.

¹³ 2008 U. S. App. LEXIS 23394, at 3–4.

¹⁴ 2008 U. S. App. LEXIS 23394, at 3–4.

judge who handled *Sullivan I*.¹⁵ All three plaintiffs sought damages for alleged violations of the California Labor Code, alleging that Oracle failed to pay overtime to employees who lived in other states, but who periodically worked full days in California.¹⁶ A second claim, essentially premised on the same allegations, was brought by all three plaintiffs under California's unfair competition law.¹⁷ Plaintiffs Evich and Burkow brought a third claim under Section 17200, based on alleged violations of the FLSA for work performed throughout the United States.¹⁸

Oracle filed a motion for summary judgment as to all three claims, which the district court granted.¹⁹ In its ruling, the lower court held that the two California statutes at issue—the California Labor Code and Section 17200—only apply to residents of California.²⁰ The district court further held that even if these statutes were construed to apply to nonresidents of California, the statutes would violate the Due Process Clause of the Fourteenth Amendment.²¹ Plaintiffs appealed.

Legal Analysis

Comparison of State Overtime Laws

The Ninth Circuit's decision in *Sullivan II* turned on its application of the choice-of-law rules of California, California imposing significantly different overtime requirements on employers than Colorado or Arizona. Under California law, an employer must pay overtime at the rate of one and one-half times the regular rate of pay to any employee who works more than 8 hours in a day or 40 hours in a week.²² The overtime rate doubles for work in excess of 12 hours in one day or for any work on the seventh day of a workweek.²³ Under federal law and the law of many other states, there is no daily overtime law;

instead, overtime is only required for work exceeding a weekly limit of 40 hours.²⁴

Businesses outside of California seemed unaffected by this change in California's wage and hour laws, unless it employed people who lived and worked within the state. Businesses, like Oracle, who employed residents of other states, applied the law of the state of the employees' domiciles. In *Sullivan II*, two employees worked in Colorado and one worked in Arizona.

Colorado does not require that overtime be paid for work exceeding 8 hours in a day,²⁵ but limits overtime pay to work in excess of 12 hours in a workday and 40 hours in a workweek.²⁶ Colorado's overtime rate of pay is limited to one and one-half times the regular rate of pay;²⁷ unlike California, it does not impose a double-time overtime rate, nor does it require the payment of overtime for work on the seventh consecutive day.²⁸

Arizona has no overtime law at all. Thus, overtime for employees in Arizona is governed solely by the FLSA. Under the FLSA, overtime is limited to one and one-half times the regular rate of pay for any work in excess of 40 hours in a workweek.²⁹ Like Colorado, the FLSA does not impose a double-time overtime rate or require overtime for the seventh consecutive day worked.

Choice-of-Law Doctrines

Applying a de novo standard of review, the Ninth Circuit applied California's choice-of-law rules, beginning with a presumption in favor of California law as the law of the forum.³⁰ A California court will *consider* whether its substantive law should be displaced by the substantive law of another state if the party seeking application of the non-California law is able to "demonstrate that the latter rule of decision will further the interest of the foreign state and therefore it is an appropriate one for the forum to apply to the case before it."³¹ If such a demonstration is made, a three step analysis is employed

to determine which of the competing laws is the more

¹⁵ 2008 U. S. App. LEXIS 23394, at 6.

¹⁶ 2008 U. S. App. LEXIS 23394, at 6–7.

¹⁷ California Business and Professions Code, section 17200 ("Section 17200")

¹⁸ *Sullivan II*, 2008 U. S. App. LEXIS 23394, at 7.

¹⁹ 2008 U. S. App. LEXIS 23394, at 7.

²⁰ 2008 U. S. App. LEXIS 23394, at 7–8.

²¹ 2008 U. S. App. LEXIS 23394, at 8.

²² California Labor Code section 510(a).

²³ California Labor Code section 510(a).

²⁴ 29 U.S.C. section 207(a)(1). For a period of time, California similarly only required the payment of overtime for work in excess of 40 hours a week, and did not impose a daily overtime requirement. On July 20, 1999, however, California Governor Gray Davis signed a law restoring the daily overtime requirement. The new law went into effect January 1, 2000. California Assembly Bill 60.

²⁵ 7 Colorado Code of Regulations section 1103-1(4).

²⁶ 7 Colorado Code of Regulations section 1103-1(4).

²⁷ 7 Colorado Code of Regulations section 1103-1(4).

²⁸ 7 Colorado Code of Regulations section 1103-1(4).

²⁹ 29 U.S.C. section 207(a)(1).

³⁰ 2008 U. S. App. LEXIS 23394, at 10.

³¹ 2008 U. S. App. LEXIS 23394, at 10.

appropriate to apply.³² First, the court evaluates whether California law and the law of the other state is “materially different.”³³ If the laws are materially different, the court then considers what interest, if any, each state has for application of its laws. The Ninth Circuit noted: “Even if there are materially different laws, ‘there is still no problem in choosing the applicable rule of law where only one of the states has an interest in having its law applied.’³⁴ Third, the court selects the law of the state whose interests “would be more impaired.” if its law were not applied.³⁵

Materially Different Laws

Comparing the laws of the three jurisdictions with a potential interest in the matter (California, Colorado and Arizona), the appellate court had little trouble concluding that the laws were “materially different.” In the process, it also concluded, contrary to the argument of Oracle, that the wage and hour law contained in California’s Labor Code applied to work done in California by nonresidents. Citing the California Supreme Court’s decision in *Tidewater Marine Western, Inc. v. Bradshaw* (“*Tidewater*”),³⁶ Oracle argued that a wage earner for purposes of the Labor Code consisted of someone who both worked and resided in California.

The *Tidewater* decision addressed the application of wage orders issued by California’s Industrial Welfare Commission as to residents working offshore in the Santa Barbara Channel. The *Tidewater* decision noted that under California law, California’s territorial boundaries extend three nautical miles beyond the outermost islands, reefs, and rocks, and include all waters between that limit and the coast. Federal law, on the other hand, defines California’s territorial boundaries more narrowly as three nautical miles from the coast. Much of the *Tidewater* opinion discusses whether the Santa Barbara Channel was subject to state or federal law. Ultimately the *Tidewater* Court decision held that, for purposes of wage laws, California’s definition of outer boundaries was controlling. Based on this finding the *Tidewater* Court stated, “[i]f an employee resides in California, receives pay in California, and works exclusively, or principally, in California, then that employee is a ‘wage earner of California’ and presumptively enjoys the protection of IWC regulations.”³⁷

³² 2008 U. S. App. LEXIS 23394, at 10.

³³ 2008 U. S. App. LEXIS 23394, at 11.

³⁴ 2008 U. S. App. LEXIS 23394, at 11.

³⁵ 2008 U. S. App. LEXIS 23394, at 11–12.

³⁶ 14 Cal. 4th 557, 1996 Cal. LEXIS 6527 (1996).

³⁷ *Sullivan II*, 2008 U. S. App. LEXIS 23394, at 14 (quoting *Tidewater*, 927 P.2d at 309).

Oracle relied on this statement to argue, by negative inference, that a nonresident is not a wage earner.³⁸ The Ninth Circuit not only rejected this argument, it found that other language in *Tidewater* supported an inference that California wage laws were intended by the legislature to apply to nonresidents working temporarily in California.³⁹ Ultimately, the court in *Sullivan II* held that “the California Labor Code is clearly intended to apply to work done in California by nonresidents.”⁴⁰

Interests of the Respective States

Citing Labor Code section 90.5(a) and, somewhat tangentially, *Lusardi Construction Co. v. Aubry* (“*Lusardi*”),⁴¹ the *Sullivan II* court held that California has a strong interest in applying its overtime rules to nonresidents working in California. Labor Code section 90.5(a) states the general policy regarding the enforcement of minimum labor standards—(1) to ensure employees are not required or permitted to work under substandard conditions or for employers that have not secured the payment of compensation and (2) to protect employers who comply with the law from those who attempt to gain a competitive advantage at the expense of those who do not comply. Although the statute does not, expressly address nonresident workers, the Ninth Circuit reasoned that “[i]f a California employer may avoid the requirements of the state Labor Code by the simple expedient of hiring nonresidents, California residents will be substantially disadvantaged in the

³⁸ 2008 U. S. App. LEXIS 23394, at 14.

³⁹ 2008 U. S. App. LEXIS 23394, at 14. The Ninth Circuit’s reasoning is somewhat attenuated. It reasoned as follows:

To the degree that any inference can be drawn from *Tidewater Marine*, it is the opposite from that drawn by Oracle. Two sentences before the sentence quoted by Oracle, the Court speculated that the legislature “may not have intended” the Labor Code to apply to “out-of-state businesses employing nonresidents, though the nonresident employees enter California temporarily during the course of the workday.” *Id.* (emphasis added). If the Court described an out-of-state employer’s employees coming into California temporarily during the course of a workday as the marginal case for Labor Code coverage, there is an inference that an in-state employer’s employees coming into California for entire workdays and workweeks is not a marginal case. That is, there is an inference that such a case comes within the Code’s coverage. 2008 U. S. App. LEXIS 23394, at 14–15.

⁴⁰ 2008 U. S. App. LEXIS 23394, at 13.

⁴¹ 1 Cal. 4th 976, 1992 Cal. LEXIS 1270 (1992).

labor market by the cheaper labor that will thereby be made available to California employers.”⁴²

The *Sullivan II* court also concluded that neither Colorado nor Arizona had an interest in applying overtime rules to its residents working out-of-state. However, for purposes of discussion it assumed that these two states had expressed such an interest and found, nonetheless, that they would support the application of California overtime laws to its residents. It stated that the economic welfare of Colorado and Arizona residents would benefit from the overtime laws in California because California law is the most advantageous to an employee. *Sullivan II* concluded by finding that California had a “strong interest” in applying its Labor Code to work performed in California, whereas Colorado and Arizona had no interest.

Comparative Impairment

Because the court found that neither Arizona nor Colorado had an expressed interest in applying overtime laws to their residents working out-of-state, there was no need to reach the third step in the analysis—the comparative impairment of interests.⁴³

Constitutional Constraints

Oracle argued that the application of California’s overtime rules to the plaintiffs’ work in California violated the Due Process Clause and the Dormant Commerce Clause of the United States Constitution.⁴⁴ The *Sullivan II* court gave short shrift to these two arguments. It noted that for a state’s substantive law to be selected in a constitutionally permissible manner, that state must have “a significant contact or significant aggregation of contacts, creating state interests, such that choice of its law is neither arbitrary nor fundamentally unfair.”⁴⁵ It easily found that there were sufficient contacts resulting from the location of Oracle’s headquarters and the performance of work by its nonresident employees in California. The court did not address whether this finding would be different if the employer’s headquarters were located in a different state, and the nonresident employees’ periodic work within California was the business’ only activity within the state.

⁴² 2008 U. S. App. LEXIS 23394, at 18.

⁴³ The ultimate finding was that California’s overtime laws applied to the nonresident plaintiffs’ claims for work performed in California. Plaintiffs maintained a companion set of claims under the Unlawful Business Practices Act (Bus. & Prof. Code section 17200). The court’s disposition of these claims directly follows its disposition of the overtime claims.

⁴⁴ *Sullivan II*, 2008 U. S. App. LEXIS 23394, at 22.

⁴⁵ 2008 U. S. App. LEXIS 23394, at 22.

As to the Dormant Commerce clause argument, the court noted that a statute will pass muster if it regulates evenhandedly to effectuate a legitimate local public purpose.⁴⁶ It held that California has chosen to apply its Labor Code equally to work performed in California, whether that work was performed by residents or nonresidents. Therefore it found no “plausible” violation of the Dormant Commerce Clause.

Commentary

This case should be carefully considered by employers hiring nonresidents to perform work in California. Even though the claims at issue in the *Sullivan II* case are limited to overtime claims, the court attributes very broad and significant policies to California’s Labor Code that could have even greater ramifications for businesses who send nonresidents to work in California.

In addition to stricter overtime laws, California also has strict laws concerning exempt employees. For example, in order to qualify for an exemption under California law, the employee must meet a minimum salary test of two times the California minimum wage.⁴⁷ Currently, California’s minimum wage is \$8.00 per hour, which means that an exempt employee must be paid a fixed monthly salary of at least \$2,773.33 before the other requirements for an exemption are even considered. It appears likely that the holding in *Sullivan II* would support a claim by nonresident employees that they are misclassified as exempt under California law, triggering a claim for back overtime, unpaid breaks, and other compensation as well as penalties and attorney’s fees.

Similarly, the trend in California of claims for unpaid rest and meal breaks could extend beyond California’s borders. In 2000, California employees became entitled to “premium pay” for missed rest and meal breaks.⁴⁸ In light of the holding in *Sullivan II*, this unique requirement under California law could be deemed to apply to out-of-state employees who work periodically within California, notwithstanding the obvious difficulty a remote employer would have in ensuring that required breaks are taken.

It is also hard to predict whether the *Sullivan II* decision will be applied to work amounting to less than a full day. None of the plaintiffs in *Sullivan II* made a claim for overtime for work involving less than a full day. Perhaps it is doubtful that an overtime claim is cognizable for less than a full day’s work; however, it is possible that labor laws other than overtime requirements could be applied to any

⁴⁶ 2008 U. S. App. LEXIS 23394, at 23.

⁴⁷ California Labor Code section 515(a), (c).

⁴⁸ California Labor Code section 226.7.

work in California, regardless of duration. California's rest and meal break requirements are one such example.

In addition to possible applications of the *Sullivan II* decision to other provisions of the California Labor Code, it is also conceivable that other courts may rely upon the holding to find that other California laws could apply to nonresident employees periodically working in the state. In order to avoid being a test case, businesses should reevaluate whether the use of nonresident employees to perform work in California is absolutely necessary or hire legal counsel to help identify employment practices that may reduce the risk of noncompliance with California's laws.

Dennis Law and Kathryn Eppright are partners in Andre, Morris & Buttery (www.amblaw.com), with offices in San Luis Obispo and Northern Santa Barbara Counties. They both specialize in civil litigation matters, including a substantive practice in the area of harassment, disparate treatment and wrongful termination. In addition, Ms. Eppright handles employment related administrative and counseling matters. The authors would like to thank Nancy Monroe for her invaluable technical assistance in the preparation of this article.