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Labor & Employment ADVISORY ■

MAY 14, 2019

Vazquez v. Jan-Pro: A Clean Sweep for Employees?

On May 2, 2019, the Ninth Circuit Court of Appeals held that the California Supreme Court's decision in *Dynamex v. Superior Court*, which applies a new test to determine if a worker is an employee or independent contractor, applies retroactively. *Vazquez v. Jan-Pro Franchising International Inc.* is a putative class action originally filed in the District of Massachusetts by a Massachusetts plaintiff and plaintiffs from several other states who alleged that Jan-Pro, a major janitorial cleaning business, had developed a "three-tier" franchising model to avoid paying its janitors minimum wages and overtime compensation by misclassifying its third-tier franchisees as independent contractors and not employees. The *Jan-Pro* matter has had a circuitous journey, with stops in Massachusetts and Georgia along the way. The Massachusetts court severed the California plaintiffs' claims from the individual claims of the lead named plaintiff, which is how this matter ended up in the District of Northern California.

The court first concluded that the res judicata and law of the case arguments made by the defendant were not well taken since the plaintiffs in the California action were not shown to have been adequately represented by the individual plaintiffs in the Massachusetts or Georgia actions. The court reiterated the rule that "one is not bound by judgment *in personam* in a litigation in which he is not designated as a party or to which he has not been made a party by service of process."

Retroactivity of *Dynamex*

On the issue of retroactivity, and its application to the plaintiffs here, the court noted that the Supreme Court of California has adhered to the general rule that decisions are given retroactive effect and that judicial decisions operate retrospectively. The *Vazquez* court acknowledged that *Dynamex* did not explicitly address the issue of retroactivity, but denied a petition by amicus parties to have the decision declared to apply only prospectively. The court noted that while the denial was not on the merits, the court's denial without comment strongly suggested that the usual retroactive application should apply to its newly announced rule. The Ninth Circuit bolstered its analysis by concluding that the California appellate court decision in *Garcia v. Border Transportation Group LLC* similarly pointed out that *Dynamex* had denied the petition on prospective application. The Ninth Circuit thus concluded that given the strong presumption of retroactivity and the *Dynamex* Court's holding that its decision was a clarification rather than a departure from established law, all factors favored the court in concluding that *Dynamex* applies retroactively.

Due Process Concern with Retroactive Application

The circuit court also held that the retroactive application of the *Dynamex* "ABC test" did not violate due process. Characterizing the *Dynamex* decision as one implicating a judicial rule rather than a legislative enactment, the court concluded that "even more deference is owed to judicial common-law developments, which by their nature must operate retroactively on the parties in the case."

Franchisor Liability Implications of *Vazquez*

The *Vazquez* decision addresses the important issue of whether franchisors such as Jan-Pro, which had no direct contractual relationship with the plaintiffs, could be considered the employer and whether the *Dynamex* ABC test should be applied. The facts regarding the franchisor model operating in this case are important to illustrate. First, Jan-Pro employed a tripartite model where it contracted with an intermediary layer of "master franchisees" who in turn contracted with a third tier of "unit franchisees" that actually provided cleaning services and operated the services on a day-to-day level. Each level was a separate corporate entity and each had its own staff. Concluding that the district court had no opportunity to apply the *Dynamex* standard and neither party had the opportunity to supplement the record, the Ninth Circuit remanded the case back to the district court to evaluate the issue on a more developed factual record. The court, however, did provide employee-friendly "guidance" to the district court, directing the district court to consider all three prongs of the ABC test.

Significantly, the circuit court held that the California Supreme Court decision in *Patterson v. Domino's Pizza LLC* was not of particular applicability since *Patterson* was not a wage and hour case, characterizing *Patterson* instead as a vicarious liability tort case. The court discounted applying the test for employee status used in *Patterson* and instead focused the district court on applying the ABC test without the "gloss" of the *Patterson* analysis that focused on establishing the right of direct control over subordinates. The circuit court instead focused on its interpretation of the California wage orders as having more to do with "creating incentives for economic entities to internalize the costs of underpaying workers."

The Ninth Circuit then pointed favorably to two Massachusetts decisions that applied the ABC test in a franchisor setting and pointed out that under an ABC scenario, a dispute between a putative employee and a hiring entity does not depend on whether they are parties to the same contract, concluding that "Jan-Pro could be Plaintiff's employer under the ABC test even though it is not a party to any contract with Plaintiffs."

The court focused on prong B of the ABC test (requiring that an employer prove it was not engaged in the same course of business as the putative employees) and provided the district court with various examples of cases where the courts concluded that the activity of the putative employees was more "necessary" than "incidental," thus militating in favor of finding an employee relationship. The court noted that "Jan-Pro is actively and continuously profiting from the performance of those cleaning services as they are being performed." The court also noted that Jan-Pro will have a hard time arguing that it does not hold itself out as a cleaning business (another factor in the B prong) and cited to several Massachusetts cases that hold that franchising is not a business in itself, with one case calling that description "a modified Ponzi scheme." Finally, the court made short shrift of the employer's attempt to use *Curry v. Equilon Enterprises* for the proposition that franchisors are in a different business, noting that the dichotomy of gasoline ownership versus "gas station operation" is less troublesome than "the business of franchising" and operating a franchise.

Takeaways

- Employers and especially California franchisors are now looking at potential liability going back four years for alleged violations of the wage and hour law in California and should examine their policies and practices to determine if members of their workforce have been misclassified under the new standard.
- Franchisors should examine their franchise agreements to determine whether their agreements pass muster with the ABC test, which will not be applied against franchisors for wage and hour claims.
- Franchisors that operate under a tripartite structure are no longer automatically insulated from wage and hour claims brought by their franchisees' employees and must reexamine their practices and agreements to distinguish themselves from their franchisees' business and the operation of their income stream.

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