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Five Key Issues Confronting Financial Services Industry Employers

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Employers in the financial services industry are faced with a growing number of employment law challenges. Whistleblower complaints are on the rise as regulatory agencies become more aggressive in their efforts to encourage employees to report alleged unlawful conduct. The Financial Industry Regulatory Authority ("FINRA") arbitration process is becoming even more unpredictable under new rules that may result in arbitration panels that are less familiar with the industry. Expanding globalization requires employers to navigate numerous immigration hurdles that arise from managing a cross-border workforce. This edition of Epstein Becker Green's *Take 5* addresses these important topics and what employers should know about them:

1. **The SEC Is Targeting Companies That Use Confidentiality Agreements That Silence Whistleblowers in Violation of the Securities Exchange Act**
2. **OSHA Has Issued Its Final Rule Governing Whistleblower Retaliation Complaints Brought Under Section 806 of the Sarbanes-Oxley Act**
3. **Internal Whistleblower Complaints Raise Important Considerations**
4. **Rule Changes Affect the Composition of Arbitration Panels in FINRA Disputes**
5. **Establishing Mobility Programs Is Essential for a Global Workforce**

1. The SEC Is Targeting Companies That Use Confidentiality Agreements That Silence Whistleblowers in Violation of the Securities Exchange Act

The Securities and Exchange Commission ("SEC") is looking closely at employment agreements, separation agreements, and other agreements that include confidentiality provisions that prevent or discourage employees from reporting possible unlawful conduct to the SEC. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") amended the Securities Exchange Act to include protections and incentives (i.e., the whistleblower "bounty" program) to encourage whistleblowers to come forward. One of the implementing regulations of the bounty program, Rule 21F-17(a), specifically prohibits

employers from taking any action that would "impede" an employee from communicating with the SEC about potential securities law violations, including enforcing or threatening to enforce a confidentiality agreement.

The SEC Cites Potential "Chilling Effects"

On April 1, 2015, the SEC announced that it had resolved its first enforcement action against a company, KBR, Inc. ("KBR"), for using overly restrictive confidentiality provisions. KBR's compliance investigators required witnesses who were interviewed during the investigation of certain types of internal complaints to sign a statement that they were "prohibited from discussing any particulars regarding [the] interview and the subject matter discussed, without the prior authorization of the Law Department" and that "unauthorized disclosure of information may be grounds for disciplinary action up to and including termination." There was no evidence that KBR ever prevented an employee from communicating with the SEC, or ever enforced the confidentiality statement to stop such communications.

Nevertheless, the SEC found that the statement violated Rule 21F-17 and undermined its purpose by forbidding employees from communicating with the SEC about the substance of an interview without KBR's permission, lest they face discipline or even termination. In a press release announcing the action against KBR, the SEC said that "any company's blanket prohibition against witnesses discussing the substance of the interview has a potential chilling effect on whistleblowers' willingness to report illegal conduct to the SEC."

For this first action, the SEC targeted a very specific type of confidentiality agreement that was being used only in the limited context of certain internal investigations. The scope of the SEC's position will likely be further developed if and when it commences actions involving severance agreements, employment contracts, or general confidentiality agreements.

The Attorney-Client Privilege

In addition, the SEC's statement does not address the lawfulness of confidentiality agreements that a witness might be asked to sign in connection with an internal investigation that is protected by attorney-client privilege. Significantly, the SEC's reference to the "chilling effect" of confidentiality provisions that prevent witnesses from discussing interviews invites inquiry into an exception built into Rule 21F-17. That exception explicitly excludes from its reach confidentiality agreements that cover information obtained through attorney-client privileged communications, unless disclosure of that information falls under another SEC rule permitting attorneys who appear before the SEC to reveal confidential client information, without company consent, in certain extreme circumstances.

When legal counsel is performing an internal investigation into alleged unlawful activity, it is standard practice to be guided by the U.S. Supreme Court in *Upjohn Co. v. United States,* 449 U.S. 383 (1981). Based on *Upjohn*, attorneys tell witnesses that the interviews are confidential and subject to the attorney-client privilege. Moreover, attorneys typically explain that for the information to remain privileged, it is important that the witnesses not share the substance of the interview with anyone. While this is often done simply as notice rather than a written agreement, sometimes witnesses are asked to sign a statement containing the *Upjohn* notice.

Thus, the SEC's position in *In re KBR, Inc.,* would not (and should not) apply as a general proscription against the use of confidentiality agreements that apply to information learned during interviews that are part of privileged internal investigations conducted by legal counsel. As recognized in the exception to Rule 21F-17—which was conspicuously unmentioned in the SEC's Order against KBR—a balance must be struck between the SEC's investigatory mission and a company's right to the attorney-client privilege.

In sum, while the full scope of the SEC's enforcement initiative remains to be seen, employers would be wise to review the confidentiality provisions in all of their agreements proactively to ensure compliance with Rule 21F-17.

2. OSHA Has Issued Its Final Rule Governing Whistleblower Retaliation Complaints Brought Under Section 806 of the Sarbanes-Oxley Act

On March 5, 2015, the Occupational Health and Safety Administration ("OSHA") issued its "Final Rule" establishing the procedures for handling retaliation complaints brought under Section 806 of the Sarbanes-Oxley Act ("SOX"). Section 806, as amended by Dodd-Frank, protects employees of publicly traded companies, as well as employees of contractors, subcontractors, and agents of publicly traded companies, from being retaliated against for reporting fraudulent activity or other violations of SEC rules and regulations. The Final Rule addresses the comments that OSHA received in response to its interim rule, issued in 2011, and sets forth the final procedures for retaliation claims under SOX, including the procedures and timeframes applicable to employee complaints and OSHA investigations. While the Final Rule does not differ substantively from the interim rule, it crystalizes the SOX whistleblower complaint procedures and reflects an increasingly whistleblower-friendly landscape.

Verbal Complaints

One of the most important aspects of the Final Rule—and a subject of considerable concern to commenters—is its adherence to the interim rule provision permitting verbal SOX complaints. Prior to the interim rule, complaints had to be in writing and include a full statement of the alleged wrongful acts or omissions. The interim rule eliminated this requirement and permitted complaints to be made verbally and reduced to writing by an OSHA investigator. Commenters argued that this procedure transforms the investigator into an advocate for the complainant, lacks any standard for the investigator's written complaint, and increases the risk that the complainant may attempt to change his or her allegations by contending that the claims were not accurately recorded by the investigator. OSHA rejected these arguments, concluding that allowing verbal complaints is "[c]onsistent with OSHA's procedural rules under other whistleblower statues."

Preliminary Reinstatement

The Final Rule also adopted the interim rule's provision on preliminary reinstatement, i.e., reinstating the complainant to his or her former position during the pendency of a dispute. Commenters had suggested—without success—that OSHA include a provision that preliminary reinstatement should not be granted if the complainant is a security risk and that OSHA articulate specific circumstances under which preliminary reinstatement is appropriate. Instead, the Final Rule provides that, if there is a reasonable basis to believe that a SOX violation has occurred, a preliminary order will be issued that provides the relief necessary to make the complainant whole, including reinstatement to the position that he or she would have had but for the retaliation.

Moreover, as an alternative to actual reinstatement, the Final Rule permits OSHA to order preliminary "economic reinstatement" during the pendency of a dispute, which allows the complainant to collect his or her same pay and benefits without having to return to work. Significantly, OSHA intentionally omitted any mechanism for employers to recover the costs of preliminary economic reinstatement if the complainant is ultimately unsuccessful on his or her claim.

Notice to Respondents

One helpful development for employers is OSHA's decision to clarify in its Final Rule the notice that respondents must receive when a complaint is filed, as well as respondents' right to receive the information that the complainant submits to OSHA during an investigation. The Final Rule expressly provides that, when a complaint is filed, OSHA must notify the respondent of the filing of the complaint, the allegations made, and the substance of the supporting evidence. The Final Rule also notes that OSHA "generally provides the respondent with a copy of its memorandum memorializing the complaint" and that the respondent can "request that OSHA clarify the allegations in the complaint if necessary." In addition, the Final Rule makes clear that, during an investigation, OSHA will ensure that each party receives a copy of all of the other parties' submissions to OSHA and is given an adequate opportunity to respond to those submissions.

In the light of these generally supportive and encouraging procedures for whistleblowers, it is more important than ever for employers to correctly identify, investigate thoroughly, and take appropriate steps to address internal whistleblower complaints before they become costly, full-blown whistleblower disputes.

3. Internal Whistleblower Complaints Raise Important Considerations

The number of whistleblower complaints is on the rise, according to the 2014 Annual Report to Congress on the Dodd-Frank Whistleblower Program, and defending against them can be costly and disrupt business operations. Taking appropriate steps in response to internal complaints can go a long way toward minimizing the risk that the issue becomes an external dispute at OSHA or in court.

Understanding the Objectives

A prompt investigation and an understanding of the objectives of the investigation are paramount. Employers should decide, for example, whether the goal is to create a factual record, prepare an investigative report addressing a particular inquiry or legal consideration, provide a basis for decision making, or serve as a defense in anticipated litigation—or any combination of these objectives. These considerations will determine whether the investigation should be undertaken by a non-attorney or by corporate counsel or outside counsel, or both.

For example, if the goal is simply to correct a problem internally, perhaps corporate counsel is appropriate. If, on the other hand, there is a high likelihood that the employee's complaint will lead to full-blown litigation, outside counsel may be more appropriate. In addition, employers must have a basic understanding of the privileges afforded to attorney work product and attorney-client communications. This is because the choice of investigator can impact whether, and to what extent, these privileges apply to the information adduced during the investigation, which, in turn, will determine whether such information will be protected from disclosure to third parties.

Whistleblowers in Compliance or Audit Functions

Employers should also know how to respond to the challenge raised by complaints made by whistleblowers who work in compliance or audit functions or are otherwise responsible for receiving and investigating internal whistleblower complaints. These "trusted" whistleblowers are especially problematic because, while they should be working to investigate and correct the issue internally, they may also decide to blow the whistle themselves and report the matter to outside authorities. Further, while they are generally ineligible for financial awards under the Dodd-Frank whistleblower bounty program, these "trusted" whistleblowers can become eligible for an award if the business takes no corrective action within 120 days after they make an internal complaint. They are also protected by anti-retaliation provisions of Dodd-Frank and SOX.

Training Managers to Receive Complaints

One of the most important considerations is making sure that supervisors and managers are trained and understand how to recognize and elevate a whistleblower complaint to the appropriate internal legal or compliance unit, and how to conduct themselves going forward to minimize the risk of a retaliation claim by an employee who blows the whistle. Issues are frequently first raised at the supervisory level, and the sooner that compliance and/or legal professionals receive information about a claim so that they can access the appropriate response, the sooner an internal investigation can commence, when necessary.

Further, managing an employee who has made a whistleblower claim can present a host of challenges, particularly if the employee is under-performing and therefore has been or is becoming a candidate for corrective or even disciplinary action. If a current employee raises a whistleblower complaint, it is essential that the alleged wrongdoing is not compounded by retaliation against that employee (or by actions that give the appearance of retaliation). Thus, supervisors and managers should receive periodic training regarding the laws and company policies prohibiting retaliation. They should also understand the need to have any potentially adverse employment actions vetted by the legal department before taking action.

Finally, supervisors and managers should be given appropriate support from the legal and/or human resources departments in terms of counseling and advice in dealing with the whistleblower on a day-to-day basis as issues arise, rather than trying to navigate these waters on their own.

4. Rule Changes Affect the Composition of Arbitration Panels in FINRA Disputes

For financial services industry employers that participate in arbitrations administered by FINRA, the composition of the arbitration panel may have as much, or more, of an impact on the outcome of the dispute than the facts or the law. This is because FINRA arbitrators are not bound to follow case precedent or strictly apply principals of law and can render awards based on their own notions of "fairness" or "justice." The important process of selecting an acceptable arbitration panel, however, can be opaque, as the information that FINRA provides about prospective arbitrators often gives limited assistance to employers trying to make informed selections. Further, recent changes to the rules affecting the composition of FINRA arbitration panels, particularly in customer cases, make it even less likely that the dispute will be heard by an experienced panel.

Current Selection Procedures

Traditionally, FINRA administrators provided all parties with three lists of arbitrators from which to select a panel: 10 "public" arbitrators, 10 "non-public" arbitrators, and 10 "public" arbitrators qualified to serve as the panel chairperson. The parties would strike a certain number of arbitrators from each list and rank the remaining arbitrators in order of preference. FINRA would then choose the highest-ranked arbitrator from the two lists to form the panel, which would consist of a "public" chairperson and two panelists, one "public" and the other "non-public."

Pursuant to a rule change that took effect on February 1, 2011, and was modified on September 30, 2013, either side in a customer dispute can designate an "all-public" panel by striking all of the arbitrators on the "non-public" list. The change may negatively impact employers because "non-public" arbitrators generally have certain defined connections to, or experience in, the securities industry and can bring an insider's perspective to bear on the dispute that may be useful in understanding an employer's position. "Public" arbitrators, on the other hand, generally have limited knowledge of securities or financial services and are perceived as being more

sympathetic to customers. In fact, according to Regulatory Notice 13-30, FINRA found that "customers were awarded damages significantly more often when an all-public panel decided their case."

New Rules

On February 26, 2015, the SEC accepted proposed changes to FINRA rules 12100(p), 12100(u), 13100(p), and 13100(u), which set forth new definitions of "public" and "non-public" arbitrators in customer and industry disputes. The new definitions significantly limit the financial industry experience a person can have and still be permitted to serve as a "public" arbitrator. Further, the rules substantially limit the circumstances under which a "non-public" arbitrator can be reclassified as a "public" arbitrator. Under former rule 12100(p) of the Customer Code (and 13100(p) of the Industry Code), there was a "cooling off" period that prohibited an individual who was classified as a "non-public" arbitrator due to his or her affiliation with certain financial services entities from becoming eligible to serve as a "public" arbitrator until five years after he or she retired from the securities industry. Under the revised rules, the "cooling off" period is eliminated and the same individual may be permanently classified as "non-public" and, therefore, ineligible to serve as a "public" arbitrator.

Employers should be aware that these new rules will significantly reduce the number of individuals who can serve as "public" arbitrators and dramatically decrease the likelihood that an assigned "public" arbitrator will have the financial industry experience and understanding that employers in FINRA disputes often seek. For customer disputes in particular, the new rules, taken together with the "all-public" panel rule, greatly increase an employer's chances of drawing a panel of inexperienced arbitrators with limited understanding of the industry. For industry disputes, where panels still must have one non-public member, the recent rule change further shifts the balance of the panel toward "public" arbitrators with no industry experience.

5. Establishing Mobility Programs Is Essential for a Global Workforce

As the economy becomes increasingly globalized, it is important for financial services industry employers to maintain their competitive edge by developing a robust toolkit of cross-border capabilities. The ability to transfer managers, executives, and other key personnel to the United States expeditiously for short-term or long-term projects or assignments is a growing business necessity. Fortunately, U.S. immigration law contains nonimmigrant (temporary) and immigrant (permanent) visa classifications specifically for managers and executives, and provides a potential fast-track to permanent residency.

Employers, however, must be careful in selecting a visa classification appropriate to the terms and conditions of employment, noting that classifications carry different tax, benefit, and short-term and long-term employment implications. Employers should also be aware of the potential mechanisms that they can utilize to facilitate the international transfer of their vital managerial and executive resource population, making short-notice transfers as quick and seamless as possible.

The L-1A Nonimmigrant Visa Program

Most often, companies transfer their managers and executives from their operations abroad to their U.S. operations through the L-1A nonimmigrant visa program. As a general rule, L-1A classification requires that (1) the U.S. and foreign entities have a qualifying parent, subsidiary, or affiliate relationship; (2) the employee has been employed abroad by the foreign entity for at least one of the last three years in a managerial, executive, or specialized knowledge capacity;

and (3) the employee will be transferring to the United States to serve as a manager or executive.

Criteria for Obtaining an L-1A Nonimmigrant Visa

To take advantage of the L-1A program, employers should carefully document their corporate organizational structure in a manner demonstrating that the size and scope of their operations warrants the services of an L-1A manager or executive. Employers that apply for an L-1A visa without a clearly documented structure may be faced with requests for additional evidence that can delay the application process substantially.

Employers should also take care in defining a manager or executive's role and responsibilities. The U.S. Citizenship and Immigration Services ("USCIS") and the U.S. Department of State tend to focus on particular factors in adjudicating L-1A applications, including whether the individual has any direct reports, budgetary authority, and discretionary decision-making authority in policy formation and/or day-to-day company operations.

While these criteria are seemingly straightforward, the financial services industry's increasing tendency toward heavily matrixed management structures does not always align with the USCIS's understanding of a personnel manager. Therefore, it is important in these cases to strengthen the managerial argument by carefully identifying a discrete and organizationally important "function" or area of operations that will be managed by the employee.

Drawbacks to L-1A Classification

When considered as part of a larger global mobility strategy, L-1A classification can have notable long-term and programmatic benefits, including:

- the possibility of an expedited green card process (foregoing the often lengthy and expensive labor certification ("PERM") process) for managers and executives who were also employed in managerial or executive positions with the qualifying entity abroad;
- the avoidance of annual quotas associated with the H-1B visa program;
- the ability to streamline the transfer of managers and executives by obtaining L-1 Blanket Petition approval from the USCIS, which reduces onboarding time by enabling employees to apply for L-1 visas directly at a U.S. Consulate or Embassy;
- high predictability for senior managers and executives so that organizations can plan for transfers and rely on set timelines; and
- the potential for keeping L-1A managers and executives transferred to the United States on a foreign payroll, facilitating relocation packages and the retention and continuity of social benefits.

Alternatives to L-1A Classification

L-1A classification is not a one-size-fits-all category, however, and the filing costs, time limitations (including an overall seven-year period of stay), and tax implications (L-1 holders are generally held to the same tax standards as U.S. citizens and green card holders) may not make business sense for managers and executives traveling to the United States on a short-term basis. In developing an internal immigration program, employers should be aware that there may be alternative solutions available, including:

- intermittent L-1A status for managers and executives who spend less than half their time in the United States during the year, which eliminates the seven-year time limitation and may lessen or eliminate U.S. income tax liability by qualifying them as nonresident aliens; and

- B-1 Business Visitor or Visa Waiver classification for managers and executives travelling to the United States on a very short-term basis to attend business meetings or conferences, participate in short-term trainings, negotiate contracts, or perform activities related to membership on a U.S. board of directors.

In sum, it is increasingly important for financial services industry employers to establish an internal immigration program to streamline the global mobility of business-critical employees as an essential tool in the cross-border toolkit. These steps can be just as vital to long-term growth as the development of cutting-edge analytics, IT capabilities, and portfolio management techniques.

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Financial Services Employment Law
NEWS, UPDATES, AND INSIGHTS FOR FINANCIAL SERVICES EMPLOYERS

Posted on July 6th, 2015 by Nathaniel M. Glasser and Kristie-Ann M. Yamane

EEOC Updates Pregnancy Discrimination Guidance

In the wake of the U.S. Supreme Court's decision in *Young v. UPS*, [1] the EEOC has modified those aspects of its Enforcement Guidance on Pregnancy Discrimination and Related Issues ("Guidance") that deal with disparate treatment and light duty.

Under the prior guidance, issued in 2014, the EEOC asserted that a pregnant worker could prove a violation of the Pregnancy Discrimination Act ("PDA") simply by showing that she was "treated differently than a non-pregnant worker similar in his/her ability or inability to work." The 2014 guidance also took the position that an employer could not refuse to offer a pregnant worker an accommodation by relying on a policy that provides light duty only to workers injured on the job. The Supreme Court, however, was highly critical of and rejected this interpretation of the PDA, finding that it would require employers who provide a single worker with an accommodation to provide similar accommodations to all pregnant workers, irrespective of other criteria.

Thus, in the Guidance the EEOC deleted that language and an entire section that discussed its interpretation of "Persons Similar in Their Ability or Inability to Work." The EEOC has updated its discussions about disparate treatment and light duty work assignments for pregnant workers by adopting the Supreme Court's holding that a plaintiff may establish a *prima facie* case of pregnancy discrimination by following the *McDonnell Douglas* burden-shifting framework (*i.e.*, by showing that she is pregnant, that she sought accommodation which was not granted, and that the employer accommodated others similar in their ability or inability to work). Further, a plaintiff may show that the legitimate, non-discriminatory reasons for the employer's actions – even if supported by a facially neutral policy – were pretextual by showing the employer's policies caused a "significant burden" on pregnant workers without reasons that were "sufficiently strong to justify the burden."

To illustrate, the Guidance states that a practice of providing light duty to a large percentage of non-pregnant employees, while failing or refusing to provide light duty to a large percentage of pregnant workers, might demonstrate that the policy significantly burdens pregnant employees. The Guidance, however, fails to specify what it considers a "large percentage," and provides no detail or examples as to what reasons might be sufficiently strong to justify such a burden.

This is the second time in two years that the EEOC has updated its enforcement guidance in this area. Last year, the EEOC revamped the Guidance to provide an overview of coverage under the PDA, to address the impact of the inclusion of pregnancy-related impairments under the Americans with Disabilities Amendments Act of 2008, and to address other benefits that must be provided to pregnant workers. These aspects of the Guidance remain unchanged.

Employers should take note of the EEOC's increased scrutiny of facially neutral policies that may impose significant burdens on pregnant workers. The EEOC's current Strategic Enforcement Plan identifies the accommodation of pregnancy-related limitations as an emerging issue that will be prioritized, and the updated Guidance on this subject is evidence of the agency's focus in this area.

[1] *Young v. UPS*, 135 S. Ct. 1338 (2015).

Wage & Hour Defense Blog
INSIGHT AND COMMENTARY ON WAGE AND HOUR LAW DEVELOPMENTS AFFECTING EMPLOYERS

The Department of Labor Addresses Independent Contractor Misclassification and Concludes That "Most Workers Are Employees"

July 16th, 2015 by Michael D. Thompson

The Administrator of the Wage Hour Division of U.S. Department of Labor has issued an Administrator's Interpretation of the FLSA's definition of "employ." And the conclusion is one that not only could have a significant impact on the way companies do business, but lead to numerous class and collective actions alleging that workers have been misclassified as independent contractors.

Addressing the misclassification of employees as independent contractors, the Administrator's Interpretation notes that the FLSA's defines the term "employ" as "to suffer or permit to work." Based on that definition, the DOL concludes that "most workers are employees."

The Interpretation cites to the six-factor "economic realities" test the DOL applies as indicia of employment, but emphasizes certain aspects of that test. Notably, the Administrator states that the goal of the "economic realities" test is to determine whether a worker is "economically dependent" on the alleged employer, or is really in business for himself or herself.

1. Is the Work an Integral Part of the Employer's Business?

The Administrator's Interpretation emphasizes that a workers' duties are likely to be an "integral part" of an employer's business if they relate to the employer's core products or services.

For example, the Interpretation cited to the Seventh Circuit's decision in *Secretary of Labor v. Lauritzen*, a self-described "federal pickle case" in which the issue was "whether the migrant workers who harvest the pickle crop of defendant … are employees … or are instead independent contractors…."

Summarizing the point, the Administrator's Interpretation quoted the Seventh Circuit's statement in that case stating that it "does not take much of a record to demonstrate that picking the pickles is a necessary and integral part of the pickle business. . . ."

2. Does the Worker's Managerial Skill Affect the Worker's Opportunity for Profit or Loss?

The Administrator's Interpretation emphasizes that the opportunity for profit or loss reflects independent contractor status only when it is dependent on managerial skill.

By contrast, the Administrator opines that the fact that a worker that can increase his or her earnings by working longer hours is not evidence that the worker is an independent contractor

3. How Does the Worker's Relative Investment Compare to the Employer's Investment?

Previously, the DOL had stated that the relative investment of a worker "compared favorably" if the investment was substantial and could be used for the purpose of sustaining a business beyond the particular job or project the worker was performing.

While these factors are mentioned in the new guidance, the Administrator's Interpretation appears to place greater emphasis on a comparison of the investments of the worker and the potential employer. The Administrator opines that even if a worker has made an investment, that investment has to be significant when compared to the investment of the purported employer.

4. Does the Work Performed Require Special Skill and Initiative?

The Administrator's Interpretation asserts that it is a worker's business skills as an independent business person, not his or her technical skills, that support independent contractor status.

The Administrator states that only skilled workers who operate as independent businesses, as opposed to being economically dependent on a potential employer, are independent contractors.

5. Is the Relationship between the Worker and the Employer Permanent or Indefinite?

The DOL's prior Fact Sheet on independent contractor status stated that the absence of a permanent relationship may not suggest independent contractor status when arising from "industry-specific factors" or the fact that the potential employer "routinely uses staffing agencies."

The Administrator's Interpretation adds to this opinion by opining that the finite nature of an independent contractor relationship should be the result of the worker's "own business initiative."

Thus, an employer who imposes limits on the duration of its independent contractor relationships should consider whether that policy will continue to have the desired results.

6. What is the Nature and Degree of the Employer's Control?

The Administrator's interpretation emphasizes that an independent contractor must control "meaningful aspects" of the work demonstrating that the worker is conducting his or her own business. However, the Interpretation does not specifically explain what aspects of a job are "meaningful."

The Administrator does make clear that flexible work arrangements are common forms of employment. Therefore, the Interpretation concludes the fact that an individual works from home or controls the hours of work is not particularly indicative of independent contractor status.

While the Administrator's Interpretation does not have the force of law (or regulation), it will be applied by the DOL and may be given deference by courts. Accordingly, employers should evaluate the extent to which they are relying on criteria addressed by the Administrator (such as flexible work arrangements and relationships of finite duration) as justification for classifying workers as independent contractors

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U.S. Department of Labor Offers New Insight on the Misclassification of Independent Contractors

July 17, 2015

By Michael S. Kun, Dean L. Silverberg, Jeffrey M. Landes, Susan Gross Sholinsky, Michael D. Thompson, Jeffrey H. Ruzal, and Judah L. Rosenblatt*

As federal, state, and local governments have focused in recent years on what they have termed "wage theft," the classification of workers as independent contractors has been the subject of agency audits and litigation (including class actions and collective actions) across the country. On July 15, 2015, the Administrator of the Wage Hour Division of the U.S. Department of Labor ("DOL") issued Administrator's Interpretation No. 2015-1 ("Interpretation") addressing how businesses should distinguish between employees and independent contractors to avoid misclassification of workers under the Fair Labor Standards Act ("FLSA").

The Interpretation may have a significant impact upon many businesses as it confirms not only that the DOL will continue to focus on the status of workers who are classified as independent contractors, but that it will do so with something approaching a presumption that "most workers are employees." And the Interpretation is likely to be used in litigation challenging the classification of workers as independent contractors.

The Interpretation refers to the FLSA's broad definition of the term "employ" and its intended expansive coverage for workers. In so doing, the Interpretation cites the DOL's "economic realities" test for indicia of employment, emphasizing certain aspects of that test.

The DOL's economic realities test typically includes six factors: (1) the extent to which the work performed is an integral part of the employer's business, (2) the worker's opportunity for profit or loss depending on his or her managerial skill, (3) the extent of the relative investments of the employer and the worker, (4) whether the work performed requires special skills and initiative, (5) the permanency of the relationship, and (6) the degree of control exercised or retained by the employer.

Notably, the Administrator states that the goal of the "economic realities" test is to determine whether a worker is "economically dependent" on the putative employer, or is really in business for himself or herself.

In the Interpretation, the DOL analyzes the "economic realities" factors as follows:

1. **Is the Work an Integral Part of the Employer's Business?**

To the extent that a worker's job responsibilities are consistent with the putative employer's business, the worker is more likely to be an employee than an independent contractor. The Interpretation emphasizes that a worker's duties are likely to be deemed an "integral part" of an employer's business if they relate to the employer's core products or services.

For example, the Interpretation cites the U.S. Court of Appeals for the Seventh Circuit's decision in *Secretary of Labor v. Lauritzen*, a self-described "federal pickle case" in which the issue was "whether the migrant workers who harvest the pickle crop of defendant … are employees … or are instead independent contractors." Summarizing the point, the Interpretation quoted the Seventh Circuit's statement in *Lauritzen* that it "does not take much of a record to demonstrate that picking the pickles is a necessary and integral part of the pickle business."

2. **Does the Worker's Managerial Skill Affect the Worker's Opportunity for Profit or Loss?**

The Interpretation emphasizes that the opportunity for profit or loss by a worker reflects independent contractor status only when it is dependent on managerial skill. By contrast, the Administrator opines that the fact that a worker can increase his or her earnings by working longer hours for the putative employer is not evidence that the worker is an independent contractor.

3. **How Does the Worker's Relative Investment Compare to the Employer's Investment?**

In previous statements, including a May 2014 Fact Sheet and a presentation on employment relationships under the FLSA on its website, the DOL indicated that the relative investment of a worker compared "favorably" if the investment was *substantial* and could be used for the purpose of sustaining a business beyond the particular job or project that the worker was performing. In the Interpretation, however, the Administrator appears to place a greater emphasis on a *comparison* of the investments made by the worker and those made by the potential employer. The Administrator opines that even if a worker has made an investment (in tools or equipment, for example), his or her investment needs to be significant when compared to the investment of the putative employer.

4. **Does the Work Performed Require Special Skills and Initiative?**

The Interpretation asserts that it is a worker's *business* skills as an independent business person, not his or her *technical* skills, that support independent contractor status. In other words, according to the Administrator, even the most skilled worker is still an employee if he or she does not know how to run a business.

5. **Is the Relationship Between the Worker and the Employer Permanent or Indefinite?**

The Interpretation states that a relationship of an indefinite (or permanent) period is evidence of an employment relationship and notes that independent contractors are typically retained on a project-by-project basis. The DOL further notes that working for other employers does not indicate a lack of "permanence."

The DOL's May 2014 Fact Sheet on independent contractor status stated that having a relationship of a defined duration does not suggest independent contractor status when arising from "industry-specific factors" or the fact that the potential employer "routinely uses staffing agencies." The Interpretation supplements this criteria by stating that the finite nature of any independent contractor relationship should be the result of the worker's "own business initiative," and not simply the fact that in the particular industry in question, engagements are usually of a short-term nature. Thus, an employer that seeks to avoid unintended employment relationships through policies that limit the duration of its independent contractor relationships should consider whether such policies will continue to achieve the desired results.

6. **What Is the Nature and Degree of the Employer's Control?**

Although control has traditionally been one of the most significant aspects of the economic realities test, the Interpretation devalues this factor. The Interpretation emphasizes that an independent contractor must control "meaningful aspects" of the work in order to demonstrate that the worker is conducting (and controlling) his or her own business. The Interpretation does not specifically explain, however, what aspects of a job are "meaningful." The Administrator makes clear that, in today's economy, flexible work arrangements are common forms of employment, and a worker is not necessarily an independent contractor simply because he or she may work outside of the putative employer's office, and set his or her own hours.

What Employers Should Do Now

Given the new guidance, employers should:

- audit their independent contractor workforce, considering the six-factor "economic realities" test and whether the contractor in question is truly in business for himself or herself;

- in connection with such an audit, consider redefining relationships with current independent contractors in a manner consistent with the Interpretation to the extent that the economic realities of the relationship more closely reflect employment status; and

- as always, consider the operational feasibility and financial implications of employing workers instead of contracting with a contingent workforce.

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***Judah L. Rosenblatt**, a Summer Associate (not admitted to the practice of law) in Epstein Becker Green's New York office, contributed to the preparation of this Advisory.*

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ACT NOW ADVISORY

NYC Commission on Human Rights Issues Enforcement Guidance for Newly Effective Credit Check Law

September 9, 2015

By William J. Milani, Dean L. Silverberg, Jeffrey M. Landes, Susan Gross Sholinsky, Kate B. Rhodes, and Nancy L. Gunzenhauser

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On September 3, 2015, the amendment to the New York City Human Rights Law ("NYCHRL") prohibiting the use of credit checks in employment ("Credit Check Law") became effective. On the same day, the New York City Commission on Human Rights ("NYCCHR"), the government agency responsible for enforcing the NYCHRL, issued enforcement guidance on the Credit Check Law ("Enforcement Guidance"), "Frequently Asked Questions," "Information for Employees and Job Seekers," and "Information for Employers."

These administrative materials from the NYCCHR expand upon and clarify certain provisions of the Credit Check Law and confirm that certain activities do not violate the Credit Check Law (e.g., performing Google and LinkedIn searches on applicants). Most significantly, the Enforcement Guidance addresses the Credit Check Law's exemptions for certain positions, including those where a credit check is required by law and high-level positions involving trade secrets, financial authority, and information technology.

The Enforcement Guidance also addresses recordkeeping practices, penalties, and the application of the Credit Check Law to workers in non-traditional roles (e.g., independent contractors).

Exemptions

As an initial matter, the Enforcement Guidance clarifies that the exemptions from the Credit Check Law apply to positions or roles, not individual applicants or employees. The Enforcement Guidance confirms that no exemption applies to an entire employer or industry.

With respect to specific exemptions, the Enforcement Guidance provides much-awaited guidance for the following:

- **Employers required by state or federal law or regulation or by the Financial Industry Regulatory Authority ("FINRA") to use an individual's consumer credit history for employment purposes.**

  The Enforcement Guidance explains that the exemption for FINRA members extends *only* to registered representatives. These FINRA members may not rely upon the exemption for other employees within the same company. In particular, the exemption does not apply to "individuals [who] perform functions that are supportive of, or ancillary to or advisory to, 'covered functions,' or engage solely in clerical or ministerial activities."

  In regard to the exemption for credit checks required by state law, the Enforcement Guidance notes that the only New York State law currently requiring an employer to consider an applicant or employee's consumer credit history applies to licensed mortgage loan originators pursuant to N.Y. Bank L. §559-d(9).

- **Positions involving responsibility for funds or assets worth $10,000 or more.**

  This exemption is limited to *only* executive-level positions with financial control over a company. The NYCCHR identifies such positions as Chief Financial Officer and Chief Operations Officer as representative examples. Importantly, the exemption does *not* include other staff members in a finance department, even if they would otherwise meet the exemption (i.e., by having responsibility for funds or assets worth $10,000 or more).

- **Non-clerical positions having regular access to trade secrets, intelligence information, or national security information.**

  The definition of "trade secrets" does *not* include the following: recipes, formulas, customer lists, processes, and other information regularly collected in the course of business or regularly used by entry-level and non-salaried employees and supervisors or managers of such employees.

- **Positions involving digital security systems.**

  Again, this exemption is limited to *only* positions at the executive level. The NYCCHR identifies such positions as a Chief Technology Officer or a senior information technology executive.

- **Positions requiring bonding under federal, state, or New York City law or regulation.**

  The following laws are examples of those that indicate positions that are required to be bonded by federal, state, or New York City law: Bonded Carriers for U.S. Customs, 19 C.F.R. § 112.23; Harbor Pilot, N.Y. Nav. L. § 93; Pawnbrokers, N.Y. Gen. Bus. L. § 41; Ticket Sellers & Resellers, N.Y. Arts & Cult. Aff. L. §§ 25.15, 25.07; Auctioneers, N.Y. City Admin. Code § 20-279; and Tow Truck Drivers, § 20-499.

- **Positions requiring security clearance under federal or state law.**

  “Security clearance” is defined as the ability to access classified information and does not include any other vetting process utilized by a government agency. The exemption applies only where the review is done by the federal or state government.

Recordkeeping

The “Information for Employers” document recommends that employers keep an “exemption log” to assist them in responding to information requests by the NYCCHR. The exemption log should include the following information:

- which exemption is claimed;
- how the applicant/employee fits into the exemption;
- the qualifications of the applicant/employee for the position/promotion;
- the name and contact information of the applicant/employee;
- the nature of the credit history information considered and a copy of such information;
- how the credit history information was obtained; and
- how the credit history impacted any employment action.

Penalties

The Enforcement Guidance clarifies that violations of the Credit Check Law may subject an employer to a penalty of up to $125,000 for violations, and up to $250,000 for violations that are the result of willful, wanton, or malicious conduct. These penalties are *in addition to* other remedies available in cases brought by individuals for violations of the NYCHRL, such as back pay and front pay and compensatory and punitive damages.

Scope of the Credit Check Law

The "Frequently Asked Questions" document provides that part-time workers, undocumented workers, interns, many independent contractors,[1] and probationary workers are all covered by the Credit Check Law.

What Employers Should Do Now

- Review job descriptions and organizational charts to determine whether any positions fit within one of the exemptions.
- Instruct recruiters and those who perform background checks to confer with legal counsel on whether consumer credit history may be used in connection with hiring or other employment-related decisions at all or for certain positions.
- Confirm that employment, placement, and temporary agencies, as well as background check providers, have revised their forms and procedures in compliance with the Credit Check Law for New York City applicants and employees.

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[1] The "Frequently Asked Questions" document does not define to which independent contractors this law would apply. The NYCHRL, however, covers "natural persons employed as independent contractors to carry out work in furtherance of an employer's business enterprise who are not themselves employers shall be counted as persons in the employ of such employer."

as an industry-focused firm, Epstein Becker Green has decades of experience serving clients in health care, financial services, retail, hospitality, and technology, among other industries, representing entities from startups to Fortune 100 companies. Operating in offices throughout the U.S. and supporting clients in the U.S. and abroad, the firm's attorneys are committed to uncompromising client service and legal excellence. For more information, visit www.ebglaw.com.

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SEC Enforcement Gives Employers a Strong Incentive to Clarify That Their Confidentiality Agreements Do Not Preclude Reporting Possible Violations of Law

April 23, 2015

By John F. Fullerton III and Jason Kaufman

The Securities and Exchange Commission ("SEC") has resolved its first enforcement action regarding a potentially overreaching confidentiality agreement following the "voluntary" revision of the agreement to state that it does not preclude employees from reporting possible violations of law.

The SEC has become increasingly vigilant and aggressive about what employers say in their confidentiality agreements and the context in which they say it. We previously cautioned employers when the Financial Industry Regulatory Authority ("FINRA") issued Regulatory Notice 14-40, which cracked down on the use of confidentiality provisions that potentially restrict employees from communicating with FINRA, the SEC, or any other self-regulatory organization or regulatory authority. After publicly announcing last fall that it would be scrutinizing confidentiality provisions, the SEC has now followed suit in *In re KBR, Inc.*, targeting overly restrictive language in one of KBR's confidentiality agreements.

Confidentiality Agreements That "Impede" External Whistleblowing

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") amended the Securities and Exchange Act to include the whistleblower incentives and protections set forth in Section 21F. Rule 21F-17 prohibits employers from taking any action to "impede" an employee from communicating with the SEC about a possible securities law violation, including enforcing or threatening to enforce a confidentiality agreement.

The SEC's Chief of the Office of the Whistleblower, Sean McKessy, indicated that his office would be analyzing and looking to bring enforcement actions with respect to severance agreements, confidentiality agreements, and employment agreements that violate Rule 21F-17(a), part of the implementing regulations of the Dodd-Frank whistleblower incentive award program (i.e., the "bounty" program).

KBR's Confidentiality Agreement in Internal Investigations

The SEC selected a very specific and particular type of agreement for its first publicized action: not a severance, employment, or general confidentiality agreement or policy, but rather an agreement that KBR's compliance investigators required witnesses interviewed in connection with certain internal investigations to sign, warning them that they could face discipline or be fired if they discussed the substance of the interview with outside parties without prior approval from KBR's legal department. KBR had begun using this form of confidentiality agreement prior to the promulgation of Rule 21F-17.

Although there was no evidence that any KBR employees were ever actually prevented from communicating with the SEC pursuant to the confidentiality agreement, or that KBR took any actions to enforce the terms of the agreement, the SEC found that KBR's use of the confidentiality agreement was unlawful because it improperly restricted employees from communicating with the SEC about the subject of an interview without KBR's permission, and it undermined the purpose of Section 21F through a threat of discipline.

"By requiring its employees and former employees to sign confidentiality agreements imposing pre-notification requirements before contacting the SEC, KBR potentially discouraged employees from reporting securities violations to us," said Andrew J. Ceresney, Director of the SEC's Division of Enforcement in the agency's press release.

Resolution of the SEC's Enforcement Action

KBR has agreed to pay the SEC $130,000 to settle the charges. Moreover, the company amended its confidentiality statement to expressly provide that it does not preclude employees from reporting possible violations of law or regulations to any government agency or from making other disclosures protected under federal whistleblower laws. The amended provision also clarifies that employees do not need KBR's authorization to make such disclosures.

This should serve as a warning that blanket confidentiality provisions that arguably forbid or impede employees from communicating with regulatory agencies, or require pre-approval to do so, may run afoul of federal law—including the False Claims Act, under which the governing view of confidentiality agreements has been similar to the SEC's position. The SEC is fully committed to prosecuting such violations, and it is very likely that additional orders will be issued in the coming months with respect to other confidentiality provisions contained in other types of agreements and/or codes of conduct. Note that the specific language that the SEC ordered KBR to use in its confidentiality agreement going forward is instructive but should not be viewed as a "safe harbor," according to Mr. McKessy.

Attorney-Client Privilege Unaffected

As we have noted previously (see Five Key Issues Confronting Financial Services Industry Employers), the KBR decision does not interfere with confidentiality agreements that are intended to safeguard privileged and confidential attorney-client communications. The SEC's statement simply does not address the lawfulness of confidentiality agreements that a witness might be asked to sign in connection with an internal investigation that is protected by the attorney-client privilege. Significantly, the SEC's reference to the "chilling effect" of confidentiality provisions that prevent witnesses from discussing interviews invites inquiry into an exception built into Rule 21F-17. That exception explicitly excludes from its reach confidentiality agreements that cover information obtained through attorney-client privileged communications.

Thus, the SEC's position with respect to the KBR confidentiality agreement would not (and should not) apply as a general proscription against the use of confidentiality agreements that apply to information learned during interviews that are part of privileged internal investigations conducted by legal counsel. As recognized in the exception to Rule 21F-17—which was conspicuously unmentioned in the SEC's Order against KBR—a balance must be struck between the SEC's investigatory mission and a company's right to the attorney-client privilege.

What Employers Should Do Now

- If your company is governed by the SEC, carefully review, and revise as necessary, all confidentiality agreements that it uses—whether in stand-alone agreements, employment agreements, separation agreements, or other policies or standards of conduct—to make certain it is clear that they do not preclude employees from reporting possible violations of law.

- If you determine that your current confidentiality provisions may conflict with the SEC's Order against KBR, consider providing notice to employees that they are not prohibited from reporting possible violations of federal law or regulation to any governmental agency or entity, including, but not limited to, the Department of Justice, the SEC, Congress, and any agency Inspector General, or from making other disclosures that are protected under the whistleblower provisions of federal law or regulation.

- Review internal whistleblowing or "escalation" policies to ensure that they, too, are in compliance with Dodd-Frank and the SEC's regulations thereunder.

- Keep in mind that different industries are subject to different regulators, which may affect the manner in which confidentiality agreements should be revised, if at all.

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Updated 50-State Wage and Hour App for Employers

Epstein Becker Green's updated version of its free, first-of-its-kind app, Wage & Hour Guide for Employers, now includes all 50 states – and more! The app puts federal and state wage and hour laws at the fingertips of employers. Plus, the updated app supports iPhone, iPad, Android, and Blackberry devices and has new capabilities.

Key features of the update include:

- New summaries of wage and hour laws and regulations covering all 50 states – plus federal law, the District of Columbia, and Puerto Rico)
- Available without charge for **iPhone**, **iPad**, **Android**, and **BlackBerry** devices
- Direct feeds of EBG's **Wage & Hour Defense Blog** and **@ebglaw on Twitter**
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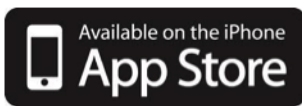

With wage and hour litigation and agency investigations at an all-time high, EBG's app offers an invaluable resource for employers, in-house counsel, and human resources personnel.

The multitude of wage and hour claims that employees have filed under the Fair Labor Standards Act and its state law counterparts has made compliance with the intricate wage and hour laws more important than ever. Employers in all industries—including financial services, health care, hospitality, retail, and technology, media, and telecommunications—are susceptible to claims under these statutes.

Rather than search through a variety of resources to locate applicable wage and hour laws, users can follow this easy-to-navigate app to find the answers to many of their questions, including citations to statutes, regulations, and guidelines. To provide the best experience possible, the app enables users to download the guide at any time, with or without a connection.

Epstein Becker Green's **Wage & Hour Guide for Employers** has been prepared by some of the most respected counselors, litigators, and authors in the field to help employers achieve their business objectives, comply with federal and state wage and hour laws, and avoid govern¬ment investigations and class action litigation.

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