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Reversing its prior position on NLRA preemption, the Ninth Circuit holds that the State of California can prohibit entities from using monies received from the State, to assist, promote or deter union organizing.

Labor Management | A Littler Mendelson Newsletter

Ninth Circuit Forbids California Employers From Using State Funds To Address Union Organizing

By John C. Kloosterman

In a divided decision with far-reaching implications, the United States Court of Appeals for the Ninth Circuit, sitting *en banc*, ruled that the State of California can forbid entities that accept state money from using that money to deter union organizing. *Chamber of Commerce v. Lockyer*, No. 03-55166 (Sept. 21, 2006). This is the third time since April 2004 that the Ninth Circuit has issued a decision in the case. The previous decisions, however, both held that California's prohibition on using state funds to deter union organizing was preempted by the National Labor Relations Act (NLRA). This latest decision will affect any entity that receives state funds or contracts with the State. In order to minimize the decision's effects, employers may want to set up separate accounting systems for money received from the State and money that comes from other sources. Such a dual system should allow employers to easily show that they have not spent any state funds on union organizing.

Background of California's Union Neutrality Law

In late 2000, in response to intensive lobbying from the AFL-CIO, the California Assembly passed Assembly Bill (AB) 1889, which expressly provides that it is California's policy to remain neutral with regard to union organizing. AB 1889 took effect on January 1, 2001 and is found at California Government Code sections 16645-16649. The neutrality law prohibits entities from using state funds to "assist, promote or deter union organizing" and potentially applies to any state contractor or grant recipient if that entity employs one or more individuals. For purposes of the law, it is irrelevant whether the employer is public or private, for-profit or not-for-profit. The specific employers covered by the neutrality law include: recipients of state grants of any amount (§ 16645.2); state contractors performing service contracts (§ 16645.3); state contractors receiving state funds in excess of $50,000 pursuant to the terms of the contract (§ 16645.4); and private employers receiving $10,000 or more in state funds in any calendar year (§ 16645.7).

All state contractors who seek payment from the State must certify that they are not seeking reimbursement for any costs incurred to assist, promote or deter union organizing (§ 16645.1). Either the California Attorney General or any taxpayer may bring suit alleging a violation of the neutrality law. Remedies for violating the neutrality law include returning the state funds used for the prohibited purpose, civil penalties, attorneys' fees and costs. Finally, if an employer commingles state funds with other funds, the neutrality law assumes that any expenditures related to union organizing were allocated between the two sources of money on a *pro rata* basis unless the employer can prove otherwise (§ 16646).

Background of *Chamber of Commerce v. Lockyer*

From the onset of the neutrality law, labor unions began to utilize it aggressively during organizing drives by filing complaints with the California Attorney General and filing lawsuits alleging that employers were using public funds in opposing organizing, forcing employers to expend time and money defending against the unions' allegations.

In response to the unions' tactics, in April 2002, the Chamber of Commerce of the United States, the Chamber of Commerce of

California, and numerous other associations and employers (collectively referred to as "Chamber") filed suit against California Attorney General Bill Lockyer seeking to have the law declared invalid. The AFL-CIO intervened on the State's behalf. On September 16, 2002, District Court Judge Gary Taylor ruled that two portions of the law, section 16645.2 (applying to recipients of state grants of any amount) and section 16645.7 (applying to private employers receiving $10,000 or more in state funds in any calendar year), were preempted by the NLRA and enjoined the State from enforcing those two sections. Judge Taylor did not rule on any of the neutrality law's other provisions because he determined that the Chamber did not have standing to challenge those provisions.

Attorney General Lockyer and the AFL-CIO appealed Judge Taylor's ruling to the Ninth Circuit, which, on April 26, 2004, issued a unanimous opinion upholding Judge Taylor's decision and finding that the California neutrality law was preempted by the NLRA. This opinion was written by Circuit Judge Fisher, who was joined on the panel by Circuit Judge Beezer and District Judge England. In addition, the National Labor Relations Board ("NLRB"), the federal agency responsible for interpreting and enforcing the NLRA, submitted a brief opining that the California law was preempted by the NLRA.

After this, the procedural history of the case becomes tortuous: On May 13, 2005, over one year after issuing its decision, the panel withdrew its opinion but did not immediately issue a replacement opinion. Several months later, on September 6, 2005, the panel issued a new opinion, written by Judge Beezer. This time, Judge Fisher, the author of the original opinion, changed his mind and wrote a dissenting opinion in favor of upholding the California neutrality law. On January 17, 2006, the Ninth Circuit voted to hear the case *en banc*, meaning it would be reheard by a panel of 15 judges, including Judges Fisher and Beezer.

The *En Banc* Decision

On September 21, 2006, the *en banc* panel released its opinion, which was also authored by Judge Fisher. With the zeal of a recent convert, Judge Fisher's new opinion holds that the NLRA does not preempt California's neutrality law.

In a nutshell, Congress intended the NLRA to federalize the field of private sector labor relations and preempt most state regulation of that field. Accordingly, the NLRA is different from federal laws such as the Fair Labor Standards Act, which provide a minimum set of employee protections that a state is free to expand upon. With the NLRA, states are not able to expand upon the statutory protections – if Congress intended the issue to be regulated by the NLRA or completely unregulated, then the states are not able to regulate at all with regard to that issue.

A court's initial inquiry in determining whether a state's action is preempted by the NLRA is whether the state action in question constitutes regulation of labor relations. If so, then the question is whether the state was acting as a market participant, i.e., was the state merely regulating in order to assure efficiency in procuring a state contract? Generally, if the state is regulating labor relations and is not acting as a market participant, then its regulation is most likely preempted by the NLRA under either the *Machinists* doctrine, which applies to state or local regulations relating to areas of labor relations law that Congress intended to leave unregulated, or the *Garmon* doctrine, which applies to regulations that are actually or arguably prohibited or protected by the NLRA.

In its original 2004 opinion, the Ninth Circuit determined that California's neutrality law constituted labor relations regulation and that California was not acting as a market participant. The court then determined that California's neutrality law was preempted under the *Machinists* doctrine because it effectively interfered with the NLRA's "system for the promotion or deterrence of union organizing."

In its 2006 opinion, the Ninth Circuit again determined that California was actively regulating labor relations and that it was not acting as a market participant. Despite that, the court held that the California law was not preempted. In reaching this decision, the court determined that the *Machinists* doctrine applies only to collective bargaining, not organizing, and that it applies only to conduct that Congress meant to leave wholly unregulated by either the NLRA or the states. Noting that the NLRB extensively regulates union organizing, the court found that it was not a field that Congress meant to leave unregulated.

Next, the court determined that the California statute also was not preempted by the *Garmon* doctrine. Section 8(c) of the NLRA regulates employer speech and allows employers to express any view so long as that view does not contain a threat of reprisal or a promise of benefit. Nevertheless, the court held that the *Garmon* doctrine does not preempt the California neutrality law because of its view that section 8(c) does not grant speech rights to employers. Accordingly, the court held that California's neutrality law is not actually or arguably prohibited or protected by the NLRA.

In reaching its ultimate conclusion, the court distinguished between a theoretical regulation that required neutrality as a condition of receiving state funds, which it implied would be problematic, and the California regulation, which contains no such condition and only applies to an employer's spending of state money. As noted below, this analysis could become important in reviewing other portions of the neutrality law.

Implications

Chamber of Commerce will affect every employer that does business with the State of California or receives grant money from the State of California. California's neutrality law is broadly drafted and appears to apply to every employer that receives $10,000 or more annually in state funds, no matter what their source. It certainly applies to any employer that receives grant money from the State or contracts with the State.

Also, *Chamber of Commerce* only involved two of the statutory provisions. However, some of the other provisions are potentially even more onerous for employers. For example, section 16645.3 flatly forbids state contractors from deterring union organizing by employees performing work on a service contract for the State or a state agency. This provision does not tie its prohibition to the receipt of state money or allow employers to use other money to deter union organizing. This provision may be unenforceable, however, in light of the Ninth Circuit's view that requiring neutrality

as a condition of receiving state funds, which is essentially what this provision requires, would likely be preempted by the NLRA.

It is also possible that other states will follow California's example and pass similar laws.

Best Practices

The California neutrality law applies to any expenditure related to union organizing, including money spent researching union organizing, or preparing for or planning any opposition to union organizing. Accordingly, employers who are subject to the law – which is any entity employing one or more persons that receives state grants, contracts with the State or receives over $10,000 in state funds through any means – must set up accounting and recordkeeping systems that account for state money separately from other money. And these separate systems must be in place prior to any union organizing. Otherwise, the neutrality law assumes that the employer has used state funds to deter organizing and the employer will have to prove otherwise. This means that if an employer does not maintain separate systems and a union sues the employer alleging improper use of state funds, the employer potentially will have to open its financial records to the union so it can prove where the expenditures related to organizing came from. With separate systems, it may be possible to provide them with only the records related to the state funds.

John C. Kloosterman is a shareholder in Littler Mendelson's San Francisco office. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com, or Mr. Kloosterman at jkloosterman@littler.com.