

FAST Act Becomes Law in California, but Voter Referendum Filed in Response

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On Sept. 5, 2022, California Governor Gavin Newsom signed into law AB 257, the controversial Fast Food Accountability and Standards Recovery Act, also known as the “FAST Act” (the Act). Its passing was swiftly met with a voter referendum filed Sept. 7, 2022, to potentially block the new law. If the proponents of the referendum collect sufficient signatures to qualify for the 2024 ballot, the Act cannot be implemented until voters decide.

With the support of the California Service Employees International Union and the Fight for \$15

organization, the Act was first introduced by California State Assemblywoman Lorena Gonzalez (D-San Diego) in January 2021, and passed by the California Senate, as amended, on Aug. 29, 2022. As stated by its supporters, the legislation is part of a multi-year effort to unionize the restaurant industry in California. With an initial focus on counter-service restaurant chains, the Act is expected to re-shape the restaurant industry in California, and may be indicative of a model for comparable bills in other industries, including retail, home health care, among others and copycat bills in other states. This GT Alert discusses the contents and potential impact of the Act post-amendment.

The FAST Act: Purpose and Impact

The Act is the product of a union-backed effort to unionize the restaurant industry. Its origins can be traced to early days of the Fight for \$15 movement, which began in 2012 with a series of fast food worker strikes in various cities around the country. These early efforts inspired numerous cities, such as Los Angeles, San Francisco, New York, Portland, and Seattle to substantially increase the applicable minimum wage, in addition to adding paid sick leave and other benefits.

Prior to the COVID-19 pandemic, the organizers' efforts to unionize restaurants were largely unsuccessful. Today, union activity has increased considerably. In the first three fiscal quarters of 2022 (October to June), union elections filed with the National Labor Relations Board are up 58% over the same period in 2021. As of the date of this GT Alert, 225 Starbucks locations have voted to unionize since a Buffalo location first voted to unionize in December 2021.

The Act failed to gain traction when first introduced in January 2021 but was reintroduced in modified form earlier this year by four Democratic assemblymembers. The Act's stated purpose is to establish a "Fast Food Sector Council" and set industry-wide standards on minimum wage, working hours, and working conditions to promote the "health, safety, and welfare" of fast-food workers in California, including by ensuring their wages align with the cost of living.

The Act's organizers, like their efforts with the Fight for \$15 movement, made large, national, franchised restaurant chains their target for promoting the legislation and rallying support behind it. However, as with the significant changes inspired by the Fight for \$15 movement, the Act likely will directly or indirectly impact all restaurants in California, and possibly beyond.

The Act defines a "Fast Food Chain" as a set of "Fast Food Restaurants" with 100 or more establishments nationally (up from the "30 or more" initially proposed) that share a common brand, or that have standardized options for décor, marketing, packaging, products, and services. The Act applies to a business that has a single location in California so long as it has 100 or more locations nationally. The Act also covers both franchised and non-franchised restaurants, meaning it covers the many businesses that own and operate some or all of their restaurant locations.

Under the Act, a "Fast Food Restaurant" is defined as a restaurant that (i) provides food or beverages, (ii) for immediate consumption on or off the restaurant's premises; (iii) to customers who order and pay for items prior to eating; (iv) with items sold or prepared in advance, including items that may be prepared in bulk and kept hot, or items that can be prepared or heated quickly; and (v) with limited or no table service.

In sum, nearly every counter service restaurant in California meets the definition of a "Fast Food Restaurant." It encompasses traditional quick service concepts, but also fast casual restaurants, certain buffet concepts, and casual dining concepts with a counter service model. Notably, the amended Act removed earlier language that the food be sold in "disposable containers or wrapping"

to meet the definition of a “Fast Food Restaurant,” potentially making the Act applicable to a growing number of concepts that do not use disposable packaging.

The Act exempts (a) bakeries that as of Sept. 1, 2022, sell bread that meets the definition of Part 136 of Subchapter B of Chapter I of Title 21 of the Code of Federal Regulations as a standalone menu item, and (b) restaurants located within “grocery establishments” (so long as the restaurant is staffed by employees of the grocer); and (c) restaurants subject to a collective bargaining agreement (i.e., a unionized location). The basis for exempting grocery establishments and bakeries in the recent amendments to the Act is unstated.

The Fast Food Council and What It Does

The cornerstone of the Act is the creation of a “Fast Food Council” whose purpose is to evaluate the adequacy of current laws and protections for Fast Food Restaurant employees and establish minimum wages, working hours, and other health and safety conditions. The Council is structured to consist of up to 10 members representing one representative from the Department of Industrial Relations; two representatives of “Fast Food” restaurant franchisors; two representatives of “Fast Food” restaurant franchisees; two representatives of Fast Food restaurant employees; two representatives of advocates for “Fast Food” restaurant employees; and one representative from the Governor’s Office of Business and Economic Development. Although, as noted above, company-owned restaurants (non-franchised) are covered by the Act, the Act does not provide for any representation on the Council for representatives from such restaurants. This omission leaves company-owned and -operated restaurants, which comprise a meaningful portion of the California restaurant industry, with no representation on a Council responsible for making decisions that will materially impact such restaurants.

The governor is responsible for appointing the representatives of the state agencies, “Fast Food” restaurant employees, “Fast Food” restaurant franchisees, and “Fast Food” restaurant franchisors. The speaker of the Assembly is to appoint one representative of advocates for “Fast Food” restaurant employees, and the Senate Rules Committee is to appoint the other representative of advocates for “Fast Food” restaurant employees. Each member of the Council is to serve a four-year term, and a Council member may not serve more than two consecutive terms.

A Council of this sort is the first of its kind in California but bears a resemblance to the Industrial Welfare Commission (IWC), which was defunded in 2004. The IWC was established to regulate wages, hours, and working conditions in different industries in California. The IWC was made up of five members, all of whom were appointed by the governor and confirmed by the Senate. The IWC had two representatives of organized labor, two representatives of employers, and one representative of the general public. The IWC published 17 Wage Orders for varying industries, which are viewed as regulations under California law.

The Council must hold meetings every six months and submit a report containing proposed standards, repeals, and amendments along with a statement of the Council’s reasons for adopting those standards, repeals, and/or amendments by Jan. 15 each year. As long as the California legislature does not take action directing otherwise, the standard, amendment, or repeal will take effect Oct. 15 of the same year.¹

Importantly, an amendment to the Act permits the Council to raise the minimum wage up to \$22 per hour in 2023 and allows the Council to increase the minimum wage based on cost of living thereafter. California’s minimum wage for 2023 is \$15.50, meaning the Council could establish an hourly wage

for “Fast Food” restaurant employees that is \$6.50 an hour higher than the current 2023 minimum wage, representing nearly a 40% wage increase.

The Senate’s Aug. 25, 2022, amendments included a provision preventing the Council from promulgating regulations creating new paid time off benefits, such as paid sick leave and paid vacation – an area many employers already invest time and expense in maintaining compliance on both a state and local level.

The Council is not officially formed until a petition approving the creation of the Council is signed by at least 10,000 California “Fast Food” restaurant employees, subject to verification requirements. The signatories must be employed by a “Fast Food” restaurant, as defined in the bill, in California at the time of signing.

Counties or cities with populations greater than 200,000 also can establish their own independent “Local Fast Food Council.” Importantly, the Local Councils cannot create standards, but may only provide written recommendations to the Council regarding state health, safety, and employment standards that they believe are “reasonably necessary.” The limitation that Local Councils make recommendations relating to state standards and not local conditions was an Aug. 25 amendment meant to ensure uniform standards across the state and avoid issues that may arise from rule variation by locality. There are 22 cities and 28 counties in California with populations over 200,000, allowing for the possibility of 50 Local Councils.

No Longer a Joint-Liability Provision

The most significant amendment to the Act was the removal of the joint liability provision, which made every franchisor covered by the Act a joint employer and liable for any labor code violations committed by its franchisees.

Pre-amendment, the Act also made any agreement that a franchisee indemnify a franchisor for liability under the Act void and unenforceable as contrary to public policy. The Aug. 25 Senate amendments also removed this prohibition.

Far-Reaching Impact

The passing of the Act will have a significant and long-term impact on the California restaurant industry, and likely restaurants and other industries in and outside of California. Proponents of the legislation have made it clear that California is a starting point, and copycat legislation may follow in other states in the not-too-distant future, as happened with the Fight for \$15 movement. California is one of the most expensive and complex states in which to operate a restaurant, and the passing of the Act may cause operators and brands to rethink business in California, including, specifically, new ways to manage labor. As costs have escalated sharply over the past several years, many companies have looked to technology to replace labor or to reduce the cost of labor. That trend may accelerate with the Act’s passage. Prices also may rise at all restaurants in California, especially if the Council votes to increase the minimum wage to \$22 an hour in 2023, or a wage within that vicinity. As the Act is drafted, the Council could propose a significant wage increase in 2023, given that wage increases are thereafter capped at 3.5% per annum commencing in 2024. A substantial wage increase will affect all restaurants in California, not just “Fast Food” restaurants, as all businesses will likely be pushed to raise wages, salaries, and benefits to be competitive with the market.

Potential Challenges to Fast Act

The FAST Act is now the subject of a referendum campaign. Opponents have 90 days from the date of the bill's enactment to collect the requisite number of signatures, based on voter turnout in previous elections, to qualify a measure for the ballot. If a referendum qualifies, the FAST Act could be stayed from being implemented until the voters decide the issue in November 2024. The likely cost of a referendum campaign for proponents and opponents combined is upwards of \$200 million.

Legal challenges based on state or federal constitutional theories of separation of powers and equal protection also may be forthcoming. Given the consequential nature of the FAST Act and the examples of other major California policy battles, such as AB 5 and the classification of workers, ongoing litigation over several years is likely from parties on all sides.

Considerations for Franchisors/Franchisees and Impact on Franchising

As noted above, the Act will directly impact both franchised and non-franchised brands with over 100 locations nationwide, but will likely have an indirect impact on chains of all sizes. The Act will impact franchisees, who are independent, small business operators who now will be subject to additional regulations, including a requirement to pay higher wages to employees than other small business operators unaffiliated with a national brand.

Franchisors nationwide, especially with California-based restaurants, typically resist the urge to implement sudden and dramatic changes to their systems while stakeholders consider political challenges in the form of a referendum and legal challenges to the Act's constitutionality. It is possible the Act will not be effective in 2023 if a referendum is successful.

That said, franchisors may wish to communicate with their franchisees to ensure they understand the Act's potential impact on their independent businesses. While the Act does not include an express provision creating a joint employment relationship between a franchisor and franchisee, franchisors must still be mindful of the potential risks associated with interjecting themselves in a way that blurs the traditional joint employment delineation such as by controlling or recommending hourly wages for employees. If the Act takes effect, franchisors should consider system-wide changes that might make it less likely they will be found to meet the Act's broad definition of "Fast Food Restaurant." For those franchised restaurants subject to the Act, franchisors and franchisees should consider operational changes designed to offset increased operating costs. These changes could include reduction in menu items; carve-outs from promotional pricing programs; increased prices for all menu items; reduction in hours of operation to reduce staffing needs; reduction of standards for minimum staffing levels; and implementation of digitalized artificial intelligence solutions to replace workers and further reduce labor costs.

FOOTNOTES

¹ There is potential for the Act to be challenged on the grounds that the Act's creation of the Council constitutes an unconstitutional delegation of legislative authority.

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