Employer Alerts!

Cumulative Index, Volume III

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Employer Alerts!

By Charles H. Fleischer, Esq.

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Supreme Court Punts on ADA vs. Seniority

The Supreme Court ruled in late April that an employer's seniority system will normally prevail over a disabled employee's interest in being assigned to a particular position. However, in "special circumstances" that the Court does not explain, the disabled person's ADA rights will trump a seniority system. The high court therefore sent the case back to the lower courts to decide whether this particular dispute was a normal case or whether it involved special circumstances.

A decision last year by the Fourth Circuit, which hears federal appeals from Maryland and Virginia, ruled that Sara Lee Corp.'s seniority system *did* preempt that company's duty to assign a disabled employee to a position for which she was otherwise ineligible. See "Intermittent Disabilities, Seniority, and the ADA," *Employer Alerts!*, March 2001, p. 4. It is now doubtful whether that case can continue to be relied on.

The Supreme Court case involved Robert Barnett, who injured his back in 1990 while working as a cargo handler for US Airways. Invoking seniority rights, he transferred to a less physically demanding position in the mailroom. Under US Airways' seniority system, Barnett's position, like others, periodically became open to bidding by employees who had greater seniority. US Airways' seniority system was not required by a union contract, but it had been in place for decades and was similar to others in the airline industry.

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In 1992 Barnett learned that two employees with seniority greater than his intended to bid for the mailroom job. He asked US Airways to accommodate his disability by making an exception to its seniority policy and allowing him to stay in the position. After considering the matter, US Airways decided against making an exception and Barnett lost his job.

Barnett then sued under the Americans with Disabilities Act, claiming that his employer's duty of reasonable accommodation under the ADA entitled him to the mailroom assignment despite his lower seniority. Barnett conceded that violations of seniority rules might constitute an undue hardship for an employer (a defense available to employers under the ADA), but he argued that US Airways had not shown any such undue hardship here.

US Airways took the opposite position, claiming that it is *never* reasonable to require an employer to violate an established seniority system. According to US Airways, a seniority system is disability-neutral, since it applies to all employees and does not create special hardships for persons with disabilities. Allowing the ADA to "trump" such rules amounts to giving preferences to persons with disabilities – a requirement not imposed by the ADA.

The Supreme Court, in an opinion by Justice Breyer, rejected both arguments. Essentially, the Court ruled that for an employee to make out a good claim under the ADA, he must show that the accommodation he was denied appears reasonable on its face. The employer then has the opportunity to show that despite its facial reasonableness, the desired accommodation in fact creates an undue burden for the employer under the employer's specific circumstances.

Addressing the seniority issue, the Court ruled that "in the run of cases" it is unreasonable to require an employer to violate a seniority system to accommodate a disability. Such systems, whether imposed under a collective bargaining agreement or unilaterally imposed by management, provide important employee benefits by creating and fulfilling employee expectations of fair and uniform treatment, job security, and predictable advancement based on objective standards.

However, said the Court, it is possible that "special circumstances" may warrant a finding that assignment to a particular job is a reasonable accommodation despite a seniority system that would otherwise forbid the assignment. If an employee could show, for example, that the employer made frequent exceptions to its seniority system, then one more departure to accommodate a disabled employee might well be reasonable. Since Barnett did not have a chance to show whether any "special circumstances" were present here, the case had to go back to the lower courts for further proceedings.

The Court's remand to give Barnett another chance to attack US Airways' seniority system makes little sense. When an employer raises seniority – or any other reason, for that matter – as its basis to deny a requested accommodation, the employee may *always* attack the proffered reason as a mere sham. Here, for example, if Barnett had evidence to show that US Airways did not in fact have a bona fide seniority system, he could have and should have presented that evidence to the lower courts. Undoubtedly, he didn't do so the first time around because US Airways's seniority system was well-established and long-standing.

If by "special circumstances" the Court meant that a seniority system could be attacked in other ways, beyond merely showing that the system was a sham, then the Court's opinion gives little guidance at all. It does not say what those special circumstances are or how they might apply.

Justice Scalia wrote a critical dissent to the decision. He accused the majority of "indulging its penchant for eschewing clear rules that might avoid litigation." According to Scalia, the Court stopped short of deciding one way or the other whether seniority systems trump ADA accommodation requests by answering "maybe."

Statutory reference. 42 U.S.C. § 12101.

Case reference. *US Airways v. Barnett*, __US__, (No. 00-1250, decided April 29, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.03.

Executive Compensation – Enough May Be Too Much!

Most business corporations, from General Motors on down, are classified as "C" corporations for federal income tax purposes. C corporations are separate taxable entities, whose taxable income is determined as one might expect – by starting with the corporation's gross revenue and deducting the cost of goods sold, salaries, rent other expenses. After paying tax on that net income, the corporation may choose to distribute some or all of what's left to its shareholders in the form a dividends. Dividends, of course, represent taxable income to the shareholders.

Because a C corporation is a taxable entity, income is taxed twice on its way through the corporation to its shareholders. One tax is paid at the corporate level and a second tax is paid at the individual shareholder level. Particularly in the case of small, closely-held corporations, where the shareholder-owners are also the directors, officers and employees, this double taxation burden is problematic.

One way to avoid double taxation is to accumulate income inside the corporation and not pay dividends. But depending on the amounts involved, the corporation may end up owing an accumulated earnings tax, which is designed to stop that very practice.

Another way to avoid double taxation is to elect S corporation status. See "S Corporation Distributions Subject to Employment Taxes," *Employer Alerts!*, Dec. 2001, p. 5. Although S corporations are generally not subject to tax as separate entities, there are restrictions on who may elect S status, and there may be undesirable tax consequences to S corporation owners.

Yet another way is to pay year-end bonuses to employee owners. Through careful calculation, the bonuses can be set so that the corporation has zero taxable income and it pays zero tax. The employee owners, of course, will owe tax on the bonuses along with whatever other compensation they receive, but that's still just one tax, not two.

(Although nonprofit, tax-exempt organizations do not have to worry about the deductibility of their compensation payments, they do need to be concerned about paying excess benefits to their board members, officers and high-level managers. See "Charitable Organizations and the Disqualified Persons Excise Tax," *Employer Alerts!*, March 2001, p. 2.)

Does this scheme work? Not always, as a recent case before the U.S. Tax Court illustrates.

Haffner's Service Stations operated a chain of discount gasoline stations in Massachusetts and New Hampshire. It also sold home heating oil in those states. Haffner's was owned by members of the family that started the business in 1940, and those owners were its directors and officers. Several of them were elderly and performed rather routine jobs for the company.

Haffner's practice was to meet with its accountants in December each year and declare bonuses based primarily on Haffner's profits for the year. These discussions never included the possibility of paying dividends. For the particular tax years in question, Haffner's paid individual bonuses (in addition to regular compensation) ranging between $250,000 and $525,000.

The IRS challenged these bonuses as unreasonable under § 162 of the Internal Revenue Code. That section allows corporations to deduct

> all ordinary and necessary expenses paid or incurred during the taxable year in carrying on

> any trade or business, including ... a reasonable allowance for salaries or other compensation for personal services actually rendered.

The taxpayer corporation has the burden of proving that its compensation payments are reasonable under § 162. And where, like Haffner's, the taxpayer corporation is controlled by the employees receiving the compensation, the facts are subject to "careful scrutiny" to be sure that the payments truly represent (deductible) compensation for services rendered, rather than (non-deductible) distributions of earnings.

In determining whether compensation is reasonable, the courts look at a number of factors, including –

- the employee's qualifications;
- the nature, extent and scope of the employee's work;
- the size and complexity of the employer's business;
- a comparison of salaries paid with the employer's income;
- prevailing rates of compensation for comparable positions in comparable companies;
- the amount of compensation paid to the employee in prior years; and
- whether the employer offers pension and profit-sharing plans to its employees.

These factors are applied on an individual employee basis, rather than in the aggregate to a group of employees. In other words, it doesn't matter that the company's overall deduction for compensation is reasonable; each individual employee's compensation must be reasonable as well.

With respect to the bonuses in question here, the Tax Court found that two of the owner employees had marginal skills and did not make any significant contribution to the success of Haffner's business. Instead, they performed only clerical, non-managerial work that could have been performed by other staff, and they devoted a substantial amount of time to separate business pursuits. Yet their compensation was substantially higher than compensation paid to other employees.

These factors, coupled with the fact that Haffner's never paid a dividend, led the Tax Court to conclude that the payments were not reasonable compensation but were really earnings distributions to shareholders. Therefore, Haffner's could not deduct the payments and had to include the payments as part of its taxable income at the corporate level. The payments were then subject to a second tax in the hands of the owner employees.

Statutory reference. 26 U.S.C. § 162.

Case reference. *Haffner's Service Stations, Inc. v. Commissioner*, T.C. Memo 2002-38 (2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 5.01.

Workers' Comp Benefits – Who's the Employer?

Union Light & Power Co., an electrical subcontractor, was hired by the general contractor, Erlich Contracting Inc. for a construction project at the Naval Research Laboratory in the District of Columbia. Union Power sent one of its electricians, Nolan Glasby, to work at the site.

At 2 p.m. one afternoon, Glasby called in his time to the owner of Union Light, indicating that he has worked his usual 8-hour day. Glasby then offered to help Erlich's project superintendent take down a mechanical winch from the roof. In the process, Glasby fell to his death.

Glasby's widow filed a claim against Union Light for statutory death benefits under the District of Columbia Workers' Compensation Act. Union Light responded that Erlich was entirely, or at least jointly, responsible for the death benefits, on the theory that Glasby was a special or borrowed employee of Erlich, or he was jointly employed by Erlich and Union Light at the time of his death.

In support of its position, Union Light argued that Glasby was engaged in a valuable service which Erlich accepted, thereby resulting in an implied contract of hire between Glasby and Erlich.

The D.C. Court of Appeals disagreed. The court started its analysis by defining "special employee" as one who is transferred for a limited time to the service of another employer. In order to show that Glasby was Erlich's "special employee" in this case, Union Light would have to prove the existence of either an express or an implied contract of employment between the two. Similar proof would be required to establish joint employment.

Here, there clearly was no express contract of employment, so the court looked to whether an implied contract existed. In other words, did Glasby, by his actions, indicate that he consented to becoming an employee – however briefly – of Erlich?

The answer, said the court, was no. Glasby did not, for example, seek Union Light's permission to perform work for Erlich, nor was there any evidence that Glasby expected to be paid for helping Erlich's project superintendent. In short, all the evidence pointed to Glasby's being a volunteer, not a special, borrowed or joint employee of Erlich.

Glasby's widow didn't lose her benefits, however. The court went on to say that although Glasby had *volunteered* to help Erlich, his doing so *arose out of and in the course of* his employment by Union Light. Therefore, Union Light, as Glasby's sole employer at the time of the accident, was responsible for death benefits under the Workers' Compensation Act.

Statutory reference. D.C. Code, § 32-1501 (2001).

Case reference. *Union Light & Power Co. v. D.C. Dept. of Employment Services*, __A.2d__ (D.C. No. 00-AA-589, decided April 25, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 7.02

Employer "Tripps" on Maryland Wiretap Act

The Maryland Wiretap Act generally prohibits the willful interception of any wire, oral, or electronic communication. One exception is where both parties to the communication consent. For that reason, the Maryland Act is known as a "two-party consent" statute. (Actually, the Maryland Act is an "all-party consent" statute, meaning that *all* parties to a communication must consent before an intercept is legal.)

Linda Tripp was charged with violating the Act because she had only one party's consent (her own) when she allegedly recorded her telephone conversations with Monica Lewinsky. Had Ms. Tripp done her alleged recording in the District of Columbia or Virginia, she would not have been charged, because those jurisdictions have one-party consent statutes, meaning that only one party to the communication need consent to the intercept. The federal statute, known as the Electronic Communications Privacy Act, is also a one-party consent statute.

Another provision of the Maryland Wiretap Act exempts "telephone equipment ... or a component thereof" – the so-called "telephone exemption" – so long as the equipment is being used in the ordinary course of business. Extension telephones and speaker phones, for example, normally qualify under this exemption, even though they can be used to intercept electronic

communication.

A question recently before the Maryland Court of Appeals was whether telephone monitoring equipment used by the Injured Workers' Insurance Fund (IWIF) fell within the telephone exemption of the Maryland Wiretap Act.

In the mid-1990's IWIF – an independent agency created under Maryland law to provide workers' compensation coverage to Maryland businesses – upgraded its telecommunications system. It installed a Meridian PBX system manufactured by Northern Telecom (now known as Nortel), to which it attached a monitoring unit manufactured by Racal. The Racal unit was used to monitor and record telephone conversations between IWIF employees and IWIF customers and workers' comp claimants. IWIF supervisors could then review those conversations at their convenience. The sole purpose of the Racal unit was to evaluate and improve customer service and to enable IWIF to resolve disputes and customer complaints.

Upon installing the Racal device, IWIF informed all its employees who would be using monitored lines as to how the system worked and the procedures and goals of the monitoring system. IWIF also made unmonitored lines available for personal calls.

Sometime after IWIF installed the Racal device, a class action suit was filed against it in Baltimore County, alleging that the monitoring system violated Maryland's Wiretap Act. Strangely, neither the Court of Appeals' opinion, nor the opinion of the lower Court of Special Appeals, explains exactly *who* the plaintiffs in the class action suit were. The only indication in the opinions is a reference to the plaintiffs' calls "to" the IWIF, suggesting that the plaintiffs were not IWIF employees but instead might have been IWIF customers or workers' comp claimants.

Both the Baltimore County trial court and the Maryland Court of Special Appeals upheld IWIF's practice, ruling that the Racal unit fell within the "telephone equipment" exemption to the Wiretap Act.

The Court of Appeals (Maryland's highest court) disagreed, holding IWIF's monitoring and recording practice illegal. According to the Court of Appeals, to be deemed "telephone equipment" a device must "further the use or functionally enhance the telecommunications system" to which it is attached. It doesn't matter whether the equipment in question was supplied by the telephone company or by some after-market vendor, nor does it matter that the equipment's sole purpose is for use with a telephone system. What matters is whether the equipment increases the effectiveness of the telephone system.

According to the Court of Appeals, the Racal equipment

> in no way increased the effectiveness of the [IWIF] telecommunications system; it may have increased the effectiveness of the monitoring and training of the IWIF employees in their interactions with the customers on the telephone, but the *telecommunications equipment itself was not improved, enhanced, or furthered by the addition of the monitoring and recording devices*. The efficiency, clarity and cost of the ... IWIF's Meridian telephone system were not positively affected by the procurement and utilization of the Racal devices.

The opinion should send chills down the spines of all Maryland companies that find it useful to record business telephone conversations for evaluation and training purposes, or simply to have a record of customer orders or instructions. Typically, companies will inform their employees in advance about a monitoring system, treating the employees' willingness to continue working for the company as consent to being monitored. In this case for example, IWIF did inform its employees about the Racal device, its purpose and operation.

Companies also include the now familiar warning to incoming callers that their phone conversations may be

monitored, again viewing a caller's willingness to proceed with the call as consent to being monitored. Whether IWIF did that here is not apparent from the court's opinion. It would have been helpful for the Court of Appeals to have mentioned the two-party consent exemption, saying that *if* IWIF had included such a warning, then its monitoring practices would have been legal. At the very least, the Court could have said it was taking no position on the effect of such a warning. In the absence of any mention at all of the Wiretap Act's two-party consent exemption, employers are left to wonder whether any monitoring system can ever be legal.

Statutory reference. Md. Code, Courts & Jud. Proc. § 10-401.

Case reference. *Schmerling v. Injured Workers' Ins. Fund*, 776 A.2d 80 (Md.App. 2000), *rev'd & remanded*, __A.2d__ (Md. No. 88, decided April 8, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 13.05.

Liability to Subsequent Employer for Misleading Reference

Does an employer have a legal duty to speak up when he knows that a departing employee has a propensity for dangerous or criminal behavior? And if he doesn't, does he face liability to a subsequent employer who unwittingly hires the employee and gets victimized?

Across the country there are few cases dealing with the question and they tend to go both ways. A recent decision by an intermediate appellate court in Washington State is illustrative.

From 1984 to 1994, Jesse Caballero worked as a custodian for Mabton School District in Washington State. During his employment he received various reprimands for joking and teasing with students. Near the end of his tenure, he was arrested and charged with three counts of child molestation. The child molestation charges arose out of a family dispute unrelated to Caballero's employment.

The Washington State prosecutor offered to drop the charges on condition that Caballero resign from his custodial job, and Caballero agreed. Because the charges were never substantiated, however, Mabton School District immediately rehired Caballero as a substitute bus driver.

Caballero later applied for a job as custodian with Richland School District. He furnished "To Whom It May Concern" recommendation letters from three Mabton officials, an example of which read –

> Jesse's custodial work was performed to a very high level of expertise. As to the calibre of efficiency in this area, I would rank him in the top 5% of all custodians that I have observed in my 33 years in education. It is with pleasure that I recommend Jesse to you as an efficient and thorough employee.

None of the letters mentioned any of the incidents involving Caballero or the since-dismissed child molestation charges.

Richland School District hired Caballero as a night custodian. After approximately two years on the job, Caballero had inappropriate, though apparently innocent, contact with a student. Richland investigated and, in the process, discovered details of Caballero's employment history at Mabton. Based on the student contact while employed at Richland and his failure to disclose the earlier incidents at Mabton, Richland fired Caballero.

Caballero filed a grievance against Richland and the matter went to arbitration. The arbitrator examined all the incidents involving Caballero. He concluded, as had the Mabton School District, that the alleged child molestation charges related to a family squabble and were

unsubstantiated. The arbitrator therefore ruled that Caballero was entitled to reinstatement. Rather than comply with arbitration award, Richland settled with Caballero and paid him some $100,000. Richland then sued Mabton for misrepresenting and failing to disclose Caballero's background.

The court ruled that Mabton was not liable to Richland. There was no evidence, for example, that Mabton's recommendation letters were inaccurate as far as they went, or that Richland relied on those letters in its hiring decision. Further, under Washington law Mabton had no duty to volunteer negative information about Caballero.

Courts in a few other states have adopted a rule of law imposing liability on one who negligently gives false information to another, where the person receiving that information reasonably relies on it and physical harm results and where the risk of physical harm was both substantial and foreseeable. Richland argued that such a rule should apply in this case. The Washington state court disagreed, saying that even if the rule were otherwise applicable, the risk of physical harm by Caballero was neither substantial nor foreseeable; in addition, Caballero did not in fact cause any physical harm.

Employers should not take much comfort from the result in this case. The court might well have ruled differently if, for example, Caballero had been convicted of child molestation, or if the molestation charges involved students. In addition, the decision of an intermediate appellate court from Washington State is not compelling precedent for courts in Maryland, Virginia and the District of Columbia. Finally, employers should realize that this is very much a developing area of the law, subject to change without advance notice.

Case reference. *Richland School District v. Mabton School District*, __P.2d__ (Wash.App. No. 20250-0-III, decided April 25, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 19.07.

Non-Compete Covenants Faring Poorly in Virginia

Last year the Virginia Supreme Court rejected as overbroad a non-compete covenant that prohibited a departing employee from working in any business "similar to" the employer's business. The problem in that case was that the non-compete covenant defined "similar to" to include companies that did not compete with the employer. See "Virginia Supreme Court Rejects Non-Compete Covenant as Overbroad," *Employer Alerts!*, Aug. 2001, p. 2. Now, that same court has refused to enforce a covenant prohibiting a departing employee from working for a genuine competitor where the employee was not personally competing with his old employer.

Most employers assume that if they draft non-compete covenants that impose *reasonable* restrictions on departing employees – that is, restrictions that are limited as to geographic area and duration and that only bar employment by direct competitors, then their covenants will generally be enforceable. Not so, says the Virginia Supreme Court.

According to the Court, some covenants are *un*reasonable on their face, but there is no such thing as a covenant that is *reasonable* on its face. Instead, no matter how reasonable the covenant may appear, the employer still bears the burden of showing, on a case-by-case basis, why his business needs that kind of protection. In the latest dispute before the Court, the employer failed to show the nature of the departing employee's new position with the competitor and therefore failed to prove that its legitimate business interests were at risk.

This past January, the U.S. District Court that sits in Alexandria had occasion to consider another restriction on departing employees.

Suppose that an employer decides to adopt a policy of prohibiting certain employees from soliciting business from the employer's customers for a period of one year following the employee's departure. Suppose further that the employer decides to impose the new policy on existing employees, as well as on employees who are hired after adoption of the policy. To implement the policy, the employer asks existing and newly-hired employees to sign a non-solicitation agreement.

Is the agreement enforceable?

With few exceptions, most courts would say yes. While all contracts, including contracts relating to employment, must be supported by "adequate consideration" – that is, both parties to the contract must get something out of the deal – most courts hold that the employee's continuing employment constitutes adequate consideration.

The District Court in Virginia ruled otherwise. Attempting to predict what the Virginia Supreme Court would rule if presented with the question (since the case called for application of state, not federal, law), the District Court said mere continuing employment is not enough. Siding with the minority of courts that have considered the question, the District Court in effect ruled that "fresh consideration" beyond mere continuing employment is required.

In those jurisdictions that require fresh consideration to support an existing employee's non-compete or non-solicitation agreement, what should an employer do? Perhaps threatening to fire non-signing employees would be enough. To be sure the agreement is enforceable, however, employers may want to go further and offer existing employees something more, like a promotion, a salary increase, or even an employment contract.

The fresh consideration issue will at some point come before the Virginia Supreme Court. Whether the U.S. District Court correctly predicted how that court will rule remains to be seen.

Case references. *Modern Environments, Inc. v. Stinnett*, __S.E.2d__ (Va. No. 011268, decided April 19, 2002); *Mona Electric Group, Inc. v. Truland Service Corp*., __F.Supp.2d__ (E.D.Va. No. 01-895-A**,** decided Jan. 30, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 14.02.

Virginia's New Whistleblower Law

Persons who go public with violations of law by their employers, particularly violations involving fraud against the government, are known as whistleblowers. In the absence of specific statutory protections, whistleblowers may find themselves out of a job, with little right to complain.

In the case of fraud by private companies against the federal government, a pre-Civil War statute known as the False Claims Act protects whistleblower employees from being fired or otherwise subjected to employer retaliation. A District of Columbia statute protects whistleblowers in connection with false claims against the District government. Maryland's whistleblower statute only protects state government employees. Until recently, Virginia has no generally applicable whistleblower statute.

This past spring, the General Assembly adopted the Virginia Fraud Against Taxpayers Act. Like its federal counterpart, the new Virginia law entitles any person (including an employee) to bring suit as plaintiff for fraud committed by a company doing business with the Commonwealth. The Virginia Attorney General has 120 days to take over the suit; otherwise, the suit proceeds in the name of the Commonwealth of Virginia with the original plaintiff in effect acting as the prosecutor. If the suit is successful, the person bringing the suit can receive a bounty of between 15% and 25% of the amount recovered, plus be reimbursed for his attorney's fees.

The new Virginia law protects the jobs of employees

who bring whistleblower suits or who just report the fraud or aid in any government investigation of the fraud.

The law takes effect January 1, 2003.

Statutory reference. Va. Code, § 8.01-216.1.

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.03.

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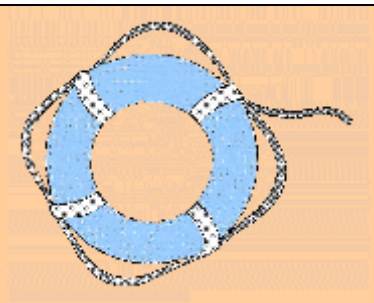

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Disabled Worker Who Is Threat to Self Not Protected By ADA

The Americans with Disabilities Act requires employers to accommodate persons with disabilities if they reasonably can. But it is alright for an employer not to accommodate based on a job-related qualification standard if the standard is "consistent with business necessary."

One illustration given by the ADA of such a permitted standard is a requirement that the disabled employee "not pose a direct threat to the health or safety of other individuals in the workplace." In other words, an employer need not hire or retain a disabled individual who, despite being able to perform the essential functions of the job, would still pose a direct threat to others.

EEOC regulations expand on that illustration by permitting employers to exclude workers who pose a direct threat to the health or safety *of the disabled individual himself* as well as others in the workplace. The question recently before the Supreme Court was whether the EEOC's interpretation of the direct threat defense is correct.

Mario Echazabal worked for a contractor at an oil refinery owned by Chevron. Twice he applied for a job directly with Chevron, which offered to hire him if he could pass the company's physical exam. Each time,

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however, the exam showed liver abnormalities, eventually diagnosed as Hepatitis C. Chevron's doctors said Echazabal's condition would be aggravated by continued exposure to toxins at Chevron's plant, so Chevron withdrew the offer. After the second physical, Chevron asked the contractor to reassign Echazabel or remove him from the plant.

The contractor complied with Chevron's request by laying Echazabal off, which prompted Echazabal to sue Chevron under the ADA. When the case got to the Supreme Court, Echazabal argued that the EEOC had no authority to interpret the direct threat defense as including a danger to the disabled person *himself*, since the language of the statute refers only to a direct threat to *others*.

In a June 10 decision, the high court disagreed, ruling that the direct-threat-to-others provision in the ADA is only an example, not a limitation. Therefore, the EEOC regulation was a valid interpretation of the ADA and Chevron acted lawfully when it refused to hire Echazabal.

Statutory reference. 42 U.S.C. § 12101.

Case reference. *Chevron U.S.A., Inc. v. Echazabal*, __U.S.__ (No. 00-1406, decided June 10, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.03.

Supreme Court Adopts "Continuing Violation" Doctrine in Hostile Environment Cases

In another June ruling, the Supreme Court said that an employee complaining of racial harassment may rely on events occurring outside the usual limitations period applicable to discrimination claims.

A discrimination claim under Title VII, which covers race, color, religion, sex, and national origin, must be filed with the EEOC within 180 days after the discriminatory conduct. (The time limit expands to 300 days for jurisdictions where there is a state or local agency comparable to the EEOC – called a Fair Employment Practices Agency – for handling discrimination complaints.) For example, if an employer refuses to hire an applicant on racial grounds, the applicant must complain to the EEOC within the 180- or 300-day period after his application is rejected.

These strict time limits are relatively easy to apply in cases where the discriminatory conduct is a specific event, such as refusal to hire, denial of a bonus, demotion, or termination. But claims based on racial or sexual harassment – so-called "hostile environment" claims – are different. In a hostile environment case, an employee suffers discrimination not because of a discrete event but because of a poisonous atmosphere in the workplace.

Claims of hostile environment discrimination often involve such things as derogatory comments, jokes, or suggestive behavior, none of which taken alone would provide the basis for suit. It is their cumulative effect, over a period of days, months, or even years, that constitutes the harassment and that creates the hostile environment.

When does the 180- or 300- time limit begins to run for hostile environment claims? The Supreme Court ruled that so long as at least one act contributing to the hostile environment occurred within the 180- or 300-day period prior to filing a charge of discrimination with the EEOC, the entire time period during which the hostile environment existed may be considered in determining employer liability. This means that an employer could be held liable for a racially or sexually hostile work environment extending over many years, so long as at least one act of harassment occurred with 180 or 300 days prior to the employee's filing an EEOC charge.

Of course, the fact that the employee tolerated an allegedly hostile environment for many years may suggest that the environment was not so hostile after all.

Statutory reference. Title VII, 42 U.S.C. § 2000e.

Case reference. *National RR. Passenger Corp. v. Morgan*, __U.S.__ (No. 00-1614, decided June 10, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.01.

Montgomery County Domestic Partner Ordinance Upheld

In 1999 the Montgomery County Council passed an ordinance to treat a domestic partner relationship the same as marriage for purposes of County employment benefits. Under the ordinance, the domestic partner of a County employee is entitled, for example, to obtain health insurance coverage as if the domestic partner were a spouse of the County employee. Leave and survivor benefits also apply.

The County reasoned that many private employers are providing, or at least plan to provide, domestic partner benefits. The County therefore needed to do so as well to compete for qualified employees. The County also saw domestic partner benefits as promoting employee loyalty and workplace diversity.

In order to qualify for County benefits, domestic partners must –

- be the same sex (heterosexual couples are not considered domestic partners under the ordinance);
- share a close personal relationship and be responsible for each other's welfare;
- have shared the same legal residence for at least 12 months;
- not be married to, or be in a domestic partnership with, any other person; and
- not be related to each other in such a way that, were they of opposite sexes, they would be prohibited from marrying.

A group of County residents attacked the ordinance on grounds that it exceeded County home rule authority, that it conflicted with state law as to who can marry, and that it violated federal law by extending COBRA and Family and Medical Leave Act benefits beyond the intended coverage of those laws.

The Maryland Court of Appeals (Maryland's highest court) has now rejected that attack and upheld the ordinance. The Court found the ordinance to be "local" rather than "general" in nature, since it only affects personnel policies within the County. Therefore, the ordinance was well within the County's authority. Further, the ordinance did not purport to regulate marriage or attempt to legitimize illegal same-sex unions – matters only the state legislature can deal with. Here, the ordinance simply defined an additional class of persons for whom County benefits were available without purporting to create a marital relationship between domestic partners.

Finally, as to argument that the ordinance unlawfully extended federal benefits under COBRA and FMLA, the Court said that those laws provide only *minimum* benefit standards and do not prohibit employers from expanding on their coverage.

In April 2000, the Virginia Supreme Court struck down a similar domestic partner ordinance, concluding that Arlington County had exceeded its authority under Virginia state law. See "Employee Benefit Coverage for Domestic Partners," *Employer Alerts!*, Jan. 2002, p. 3.

Regulatory references. Mont. Cnty. Code, §§ 19A-4, 33-22.

Case reference. *Tyma v. Montgomery County*, __A.2d__ (Md. No. 20, decided June 14, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.**

19.02.

Red Cross May Fire Employee for Reporting Blood-Handling Violations

Although an at-will employee can be fired for any reason or for no reason, he cannot be fired for a "bad" reason. Among the bad reasons is a firing that is contrary to some important, well-established public policy. Such firings are known as "abusive" or "wrongful" and provide a basis for an employee to sue. See "Wrongful Termination Update," *Employer Alerts!*, Oct. 2001, p. 1.

In two recent Maryland cases, the employees each claimed that their termination was abusive. In each case the employee lost.

In one case, an employee of the Red Cross telephoned the organization's hotline to report alleged violations of FDA regulations and a federal court decree relating to blood bank services. The employee was suspended because of the call and was fired two weeks later.

The employee then brought suit in federal court. The U.S. Court of Appeals for the Fourth Circuit (which hears federal appeals from Maryland and Virginia) ruled that under Maryland law, the termination was not abusive. The court pointed out that in order for a public policy to be well-established enough to form the basis for a wrongful discharge action, there must be –

> a preexisting, unambiguous, and particularized pronouncement, by constitution, enactment, or prior judicial decision, directing, prohibiting, or protecting the conduct in question so as to make the public policy on the relevant topic not a matter of conjecture or interpretation.

According to the court, there was no reason to believe that *federal* policy, embodied in FDA regulations and federal court decrees, constituted part of *Maryland* public policy.

Two weeks after the Red Cross decision, the Maryland Court of Appeals (Maryland's highest court) dealt with the claim of a security guard who was fired by Sears Roebuck after investigating and reporting suspected theft by a Sears store manager. The court ruled that Maryland *does* have a public policy encouraging employees to report criminal conduct, but the report must be to law enforcement officials. In the case before the court, the security guard's report was only to supervisors within the Sears organization. Therefore, Sears was free to terminate the guard without violating Maryland public policy.

Case references. *Szaller v. American Nat. Red Cross*, __F.3d __ (4th Cir. No. 01-2014, decided June 5, 2002); *Wholey v. Sears Roebuck* & Co., __A.2d__ (Md. No. 105, decided June 19, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.03.

Quitting to Take Better Job Not "Good Cause" for UI Benefit Purposes

State unemployment insurance programs are intended as safety nets for employees who lose their jobs through no fault of their own. If an employee is fired for misconduct, he may be disqualified from receiving benefits for various time periods, depending on the degree of misconduct. See "Unemployment Insurance Benefits and Misconduct," *Employer Alerts!*, Nov. 2000, p. 3.

Normally, if an employee voluntarily quits, he is not entitled to benefits either. But the unemployment insurance statutes in all three local jurisdictions provide that the disqualification only applies if the employee leaves

work "without good cause." Stated another way, if an employee voluntarily quits *with* good cause, he is not disqualified and may receive benefits.

What do the statutes mean by "good cause"? A recent Maryland case explains.

Patrick Plein was employed by Atlas Tile & Terrazzo as a tile setter's helper, at $9.00 per hour. In mid-August 2000 he was offered and accepted a job at Home Depot's Ellicott City store as a sales associate. The Home Depot job paid $12.00 per hour and provided substantial fringe benefits. After about a month on his new job, Plein was unexpectedly laid off through no fault of his own. He then applied for unemployment insurance (UI) benefits.

Under Maryland's UI law, all employers for whom a UI claimant worked during his "base period" can be charged with for benefits paid to the claimant. A claimant's "base period" is the first four of the last five completed calendar quarters immediately preceding the start of the benefit year. But if a claimant separated from any base period employer for a disqualifying reason, then the claimant is disqualified from receiving any benefits. So the question for Plein was whether his separation from Atlas Tile to take a better job with Home Depot was "for cause".

The Maryland Court of Appeals began its analysis with the UI statute itself. The statutory definition says that the cause must be "directly attributable to, arising from, or connected with ... the conditions of employment ... or the actions of the employing unit." (The District's UI statute has a similar good-cause-connected-with-work requirement. Virginia's statute doesn't say "connected with work" but it does say that good cause does not include leaving to become self-employed or leaving to join or accompany a spouse in a new locality.)

The Maryland court concluded that leaving to take a better job is not good cause, because it is unrelated to the job the employee is leaving. Instead, it is a purely personal reason, as would be leaving to relocate with a spouse, or to return to school.

Statutory references. Md. Code, L&E § 8-1001; Va. Code § 60.2-618; D.C. Code § 51-110.

Case reference. *Plein v. DLLR*, __A.2d__ (Md. No. 116, decided June 12, 2002); *Total Audio-Visual Systems, Inc. v. DLLR*, 758 A.2d 124 (Md. 2000).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 8.03.

Who Are "Employees" Under Federal Labor Law?

The National Labor Relations Act offers a variety of protections to employees. See "Labor Law Protections in Non-Union Shops," *Employer Alerts!*, Feb. 2002, p. 6. The Act defines "employee" in an unhelpful, circular way – "the term 'employee' shall include any employee" – although it goes on to exclude from the definition various specific groups, such as agricultural laborers, domestic workers, individuals employed by their spouses or parents, independent contractors, and supervisors. In separate cases handed down this June, the U.S. Court of Appeals for the D.C. Circuit explains who does and does not fit within the Act's definition of "employee".

Employee vs. independent contractor

Corporate Express Delivery Systems engaged two types of drivers to deliver packages in Oklahoma City – those who drove company vehicles and those who operated their own vehicles. The Company considered the first type as employees, but it treated owner-operators as independent contractors.

When several of the owner-operators began holding meetings to discuss forming a union, the company spied on them, it threatened to close its Oklahoma City branch, and it fired three of the union organizers. The company's actions would clearly be illegal under federal labor law if the owner-operators were employees for labor law

purposes, but if they were only independent contractors, there would be no violation.

In concluding that the owner-operators should be classified as employees, the Court of Appeals (acting at the urging of the National Labor Relations Board) approved a new guideline for distinguishing employees and independent contractors. Traditionally, the test turns on whether the employer exercises, or has the right to exercise, control over the way the worker performs his job. Under the new guideline, the test now is whether the worker "has a significant entrepreneurial opportunity for gain or loss." Stated another way, who takes the economic risk connected with the worker's job – the company or the worker? If the risk is with the company, then the worker should be classified as an employee. But if the worker bears the risk, then he's an independent contractor.

Applying this new test to Corporate Express Delivery's owner-operators, the Court observed that the company prohibited them from employing others to do the company's work and it also prohibited them from using their vehicles to deliver packages for others. This, said the Court, made them employees, not entrepreneurs.

Temporary and seasonal workers

Ordinarily, the National Labor Relations Board uses a simple formula to determine who is eligible to vote in a representation election: workers are eligible if they are employed on the date of the election itself and if they also were employed during the payroll period preceding the Board's order that the election take place. However, in determining who has sufficient continuity and regularity of employment to be included in the bargaining unit, the Board sometimes has to tailor its usual formula to fit varying employment situations.

Temporary and seasonal workers present just such a situation.

King Curb is a sheet metal fabricator, supplying fittings for use by construction contractors as part of skylight, ventilation, and similar systems. Although King Curb operates year-round, it experiences seasonal fluctuations. So as orders slow in wintertime, the company typically lays off many of its employees.

In a representation election held on January 2001, 13 employees were then working and eligible to vote. In addition, the Board ordered that all laid-off employees who had worked a minimum of 15 days in either of two 3-month periods preceding the election had a reasonable expectation of recall and were therefore eligible to vote. This formula resulted in another 27 individuals being eligible.

The Court of Appeals rejected the Board's formula. The Court pointed out that the additional employees had been hired only for a very brief period to meet a short-lived spike in demand. King Curb had no plans to increase production to levels so as to justify recalling the former employees, nor was it King Curb's practice to re-employ laid off employees. The Court was particularly critical of the effect of the formula in this case – to swell eligibility from 13 to 40 employees.

The Court sent the case back to the Board either to explain its decision or to develop an eligibility formula properly tailored to the facts of the case.

Statutory reference. 29 U.S.C. § 152.

Case references. *Corporate Express Delivery Systems v. NLRB*, __F.3d__ (D.C. Cir. No. 01-1058, decided June 11, 2002); *King Curb v. NLRB*, __F.3d__ (D.C.Cir. No. 01-1247, decided June 7, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 19.08.

IRS's "Aggregate Estimation" Method for Tips Upheld

Tips, along with other forms of compensation, are subject to FICA tax. In order for employers to calculate and pay the tax, their employees are obligated to report the amount of tips they receive. It is common, however, for employees to under-report their tips. So the IRS has developed a number of techniques to assure payment of all taxes due.

One IRS technique is known as the "aggregate estimation" method. For example, in 1991 and 1992, the Fior D'Italia restaurant in San Francisco remitted FICA tax based employee-reported tips of $247,181 and $220,845. For those same years, however, customer credit card slips showed tips of $364,786 and $338,161 – far more than the employees had reported. The discrepancy led to an IRS compliance check and an assessment against Fior D'Italia for additional FICA tax.

The way the IRS computed the additional assessment was very simple. Based on an examination of the restaurant's credit card slips, the IRS concluded that customers tipped, on average, 14.49% in 1991 and 14.29% in 1992. Assuming that cash-paying customers tip at the same rate as credit card customers, the IRS calculated total tips of $403,726 for 1991 and $368,374 for 1992. Subtracting the tips previously reported, the IRS assessed FICA tax on the difference.

Fior D'Italia objected to the methodology. It claimed the IRS had to begin at the individual employee level by determining the tips each employee received, adding all tips together, and then assessing the tax on the resulting total. That approach would obviously be far more burdensome on the IRS and, in all likelihood, yield a smaller tax.

The question before the Supreme Court was whether the Internal Revenue Code authorizes the IRS to use the aggregate estimation method of assessment. In a 6 to 3 decision, the Court approved the IRS's approach.

Under the Code, the IRS

> is authorized and required to make the inquiries, determinations, and assessments of all taxes ... which have not been duly paid.

That provision, said the Court, necessarily grants the IRS power to decide how to assess. And sometimes the IRS has no choice but to estimate tax liability, where for example no returns have been filed or records have been destroyed. The only constraint is that the estimation method be reasonable.

In this case, argued Fior D'Italia, the method was unreasonable. According to Fior D'Italia, there is no proof that cash customers tip at the same rate as credit card customers. Some customers also stiff waiters by leaving no tip at all. And some customers may charge a large tip on their credit card, but ask for some cash back. Recognizing these possibilities, the Supreme Court nevertheless found the aggregate estimation method reasonable. The Court pointed out that restaurants are free to show that the method is inaccurate in any particular case. Further, the restaurants are in the best position to track the type of information that Fior D'Italia complained made the method unreasonable.

Restaurants like Fior D'Italia are in a difficult position. On the one hand, they are entitled to rely on employee reports, despite knowing full well that some employees under-report. On the other hand, they are subject to being assessed for FICA tax based on unreported tips.

The IRS has attempted to address these complaints by developing its "Tip Reporting Alternative Commitment" whereby a restaurant promises to establish accurate tip reporting procedures in return for an IRS promise to assess FICA tax on reported tips alone. Still, restaurants do not like to act as tax police over their employees and they argue that the IRS has used the aggregate estimation method to coerce restaurants into participating in the Tip Reporting Alternative Commitment program.

Congress has been sympathetic to the restaurants' plight. For one thing, Congress included in the Internal Revenue Service Restructuring and Reform Act of 1998 a prohibition against IRS threats to audit a restaurant in an attempt to coerce it into the tip reporting program. Second, federal tax law allows restaurants a dollar-for-dollar credit against their own income tax for any FICA tax they pay on employee tips. Finally, penalties and interest don't begin to run for FICA tax on unreported tips until the IRS actually assesses the amount it claims is due.

Still, restaurants feel they are singled out for IRS abuse. The Supreme Court's latest decision is unlikely to relieve their concerns.

Statutory reference. 26 U.S.C. § 3101.

Case reference. *United States v. Fior D'Italia, Inc.*, __U.S.__ (No. 01-463, decided June 17, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 5.02.

No Private Right of Action Under FICA

In the traditional employer-employee relationship, the employer withholds the employee's share of FICA from the employee's paycheck (currently 6.2% of the first $84,900 in compensation). The employer then matches the amount withheld and remits a total of $10,527.60 to the IRS. See "Social Security (F.I.C.A.) Withholding Changes for 2002," *Employer Alerts!*, March 2002, p. 7.

For self-employed independent contractors, there is no employee withholding and no employer match. Instead, the independent contractor himself pays a self-employment tax equal to the entire $10,527.60.

Suppose an employer incorrectly classifies a worker as an independent contractor when, in reality, the worker should have been treated as an employee. Does the worker have a claim against his employer for the $5,263.80 that the employer should have matched but didn't?

Craig McDonald worked as an insurance agent and agency manager for an office of Southern Farm Bureau Life Insurance Company in Rome, Georgia. His contract with Southern Life classified him as an independent contractor and expressly negated any employer-employee relationship. Consistent with McDonald's independent contractor status, Southern Life withheld nothing from McDonald's compensation checks and it made no FICA contributions on McDonald's behalf. This left McDonald responsible for paying 100% of his FICA obligation.

Despite his contract, however, McDonald claimed that Southern Life exercised substantial control over his activities by regulating his hours, dictating the manner in which he sold insurance products, regulating his advertising, and providing him with an office, supplies, and support staff. This, said McDonald, made him an employee, no matter what the contract said.

So McDonald sued, asking the federal courts to recognize his true status as an employee and to force Southern Life to pay its share of FICA. The case eventually came before the U.S. Court of Appeals for the 11th Circuit. The court ruled that the Federal Insurance Contribution Act is a tax statute that only the federal government can enforce. According to the court, Congress did not intend to create a private right of action by persons like McDonald.

The 11th Circuit went on to point out that McDonald was not without a remedy. Under federal tax laws and regulations, he could –

- file form SS-8 asking the IRS to determine whether he is an employee or an independent contractor for federal tax and withholding purposes;

- file an administrative claim with the IRS asking for refund of the FICA taxes he allegedly overpaid;
- sue for a refund in federal court; or
- initiate an administrative action before the Social Security Administration to correct his social security records.

Statutory reference. 26 U.S.C. § 3101.

Case reference. *McDonald v. Southern Farm Bureau Life Ins. Co.*, __F.3d__ (11th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 5.02.

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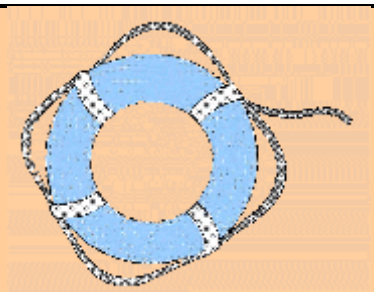

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Employee Handbooks as Employment Contracts

Employee handbooks are valuable workplace tools. They promote uniformity in treatment of employees, particularly for larger employers with several layers of management. That in turn improves morale and frees the employer from a stream of requests for special treatment.

Handbooks are also a handy source of information for job applicants and new hires, as well as existing employees. They promote efficiency and they help to establish an institutional culture. They set out rules of workplace behavior which, if willfully violated and result in termination, provide the employer with a defense to an unemployment insurance claim or an abusive discharge suit. Finally, they provide evidence of employer compliance with law in areas such as workers' compensation, equal employment, and sexual harassment.

But handbooks have their downside. Courts sometimes view them as implied contracts, in effect converting an employment-at-will relationship to a contractual relationship that limits an employer's right to fire. Two recent District of Columbia cases show how this can happen.

Dantley v. Howard University

Paulette Dantley worked for Howard University as an admissions assistant. Upon employment she received a non-faculty employee handbook. After she had worked there for six years, the University informed Dantley that her position was being eliminated. Dantley

In this issue ...

then sued, claiming that the handbook amounted to a contract of employment and that the University could not simply eliminate her position.

The University responded to Dantley's suit by pointing out that the handbook contained the following disclaimer: "This document is not to be construed as a contract." According to the University, that disclaimer alone was sufficient to warrant dismissal of the suit without any trial. The University further relied on a 1999 D.C. Court of Appeals decision involving the *very same employee handbook*, in which the Court said in a footnote, "The employee handbook clearly states that it is not an employment contract. That ends the matter."

The trial court agreed with Howard University and dismissed Dantley's suit. But the D.C. Court of Appeals (the same court that in 1999 said, "That ends the matter") reversed. The Court disposed of its 1999 footnote by saying that the footnote was not an essential part of the 1999 decision – that it was, in legal terms, mere *dicta* or surplusage. The Court then said a disclaimer alone is not enough. The handbook must go on to contain language "clearly reserving the employer's right to terminate at will." Further, said the Court, other provisions of the handbook dealing with disciplinary matters limit the circumstances under which Howard can terminate employees. Therefore, the disclaimer was at odds with other handbook provisions and it

> do[es] no more than produce the kind of ambiguity that creates a jury question as to whether the handbook constitutes a promise of continued employment to employees terminable only for cause in accordance with its provisions.

In short, the case had to go back to the trial court for a determination – presumably by a jury – whether the handbook as a whole was intended as a contract of employment.

Brown v. George Washington University

The second case, decided by the same D.C. Court of Appeals, also involved a university employee. There, however, the university *complied with* its handbook (which it called a Faculty Code) when it took adverse action against the employee. For that reason, the Court upheld the university's actions.

The employee in the case, Carole Brown, was an assistant professor at George Washington University. She initially had a three-year employment contract, but when the contract expired, GW did not renew it. Even before the contract expired, GW removed Brown as principal investigator under a grant project she was working on.

Brown claimed that in acting as it did, GW failed to follow grievance procedures spelled out in the Faculty Code. The Court disagreed. Implicitly assuming that GW was bound to follow Faculty Code procedures, the Court reviewed at length the steps GW took to do so, including providing Brown with a full hearing on her grievance. Brown's appeal, said the Court, must fail because she simply had not shown any lack of substantial compliance with Faculty Code procedures.

In an interesting sidebar, the Court observed –

> In the context here, we proceed with particular caution, recognizing that courts should not invade, and only rarely assume academic oversight, except with the greatest caution and restraint, in such sensitive areas as faculty appointment, promotion, and tenure, especially in institutions of higher learning. Where a university has adopted rules or guidelines in such areas, the courts will only intervene where there has not been substantial compliance with those procedures.

One wonders whether this observation offers reliable guidance for future cases, or is merely gratuitous *dicta* to be ignored as the Court did in *Howard University v. Dantley*.

* * * * *

An employer who wishes to adopt an employee handbook but who does not want to be contractually bound by its provisions can take steps to reduce, if not eliminate, the risk of contractual liability. Consider –

- ! including prominent disclaimers that the handbook is not a contract of employment and is not intended to change the at-will status of any employee;
- ! stating that the handbook is intended only as a convenient source of information about the company and its current practices and procedures, which are subject to change at any time without prior notice;
- ! stating that employees are free to resign at any time and that the company is free to discharge an employee at any time, with or without cause;
- ! stating that the company is not bound to follow any particular disciplinary procedures and that the company need not be consistent in imposing discipline;
- ! avoiding statements such as the company "promises" or "guarantees" or "will" take specified action in certain circumstances; and
- ! avoiding any requirement that employees sign an agreement to comply with or be bound by the handbook.

It may not be practical, at least in an academic setting involving tenured faculty, to disclaim any contractual obligations and retain power to fire at will. In that circumstance, employers should take care to draft reasonable disciplinary procedures that are fair to employees without placing overly burdensome requirements on the employer. Employers also need the freedom to act quickly in emergencies where, for example, fellow employees or students face significant risk of harm. Finally, employers need to *comply with* whatever procedural requirements they have chosen to impose on themselves.

Case references. *Dantley v. Howard University*, ___A.2d___, 2002 WL 1378247 (D.C. 2002); *Brown v. George Washington University*, ___A.2d ___, 2002 WL 1475107 (D.C. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.05.

Transgender Discrimination

Title VII of the federal Civil Rights Act and most state and local fair employment laws prohibit discrimination "because of ... sex." Although these laws cover a variety of gender-based adverse employment actions, court interpretations place limits on their applicability. For example, Title VII does not protect against sexual orientation discrimination. See "Sexual Orientation Discrimination Under Title VII," *Employer Alerts!*, April 2001, p. 4. (Note, however, that many state and local laws *do* cover sexual orientation discrimination. See "Maryland Expands Employment Discrimination Protections," *Employer Alerts!*, June 2001, p. 2.)

One topic that has received little attention in the courts is transgender discrimination. A recent decision by the U.S. Court of Appeals for the Eighth Circuit (which includes Minnesota), does address the issue.

David Nielsen, a male, began working for a school district in Minneapolis in 1969. Nearly thirty years later he informed school administration that he identified with and was adopting the opposite gender and would transition from male to female. Thereafter, he would be known as Debra Davis.

Among the issues facing the school district was which restroom facilities Nielsen-Davis would be permitted to use after transition. Upon review of Minnesota's Human Rights Act, which prohibits discrimination based on a person's "self-image or identity not traditionally associated with one's biological maleness

or femaleness," attorneys for the school district advised that Nielsen-Davis should be permitted to use the women's faculty restroom.

Carla Cruzan, a female teacher at the school, complained that Nielsen-Davis's use of the female facilities amounted to religious and sex discrimination against *her*. The Court of Appeals disagreed on a number of grounds.

First, as to the claim of religious discrimination, the Court said that Cruzan had failed to complain on time. The claim was also substantively defective because all Cruzan could show was inconvenience – she had to use another, more distant restroom to avoid encountering Nielsen-Davis – which did not amount to an adverse employment action.

As to her sex discrimination claim, Cruzan had the burden of showing that the school was "permeated with discriminatory intimidation, ridicule and insult." Since a (hypothetical) reasonable person would not have found the school environment hostile or abusive, said the Court, Cruzan's sex discrimination claim must fail as well.

The more interesting question, not addressed by the Court, is whether Nielsen-Davis would have had a claim of sex discrimination had he/she been denied access to the women's restroom.

Statutory reference. Title VII, 42 U.S.C. § 2000e.

Case reference. *Cruzan v. Minneapolis Special School District*, ___F.3d___, 2002 WL 1339108 (8th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.03.

Unfair Labor Practice Update

Federal labor law not only regulates relations between companies and unions, it also protects employees in non-union shops as well. See "Labor Law Protections in Non-Union Shops," *Employer Alerts!*, Feb. 2002, p. 6. That article describes a number of unfair labor practices of concern to all employers, whether or not their workforces have been formally unionized. Here are some more.

Confidentiality rules. The Phoenix Transit System had a confidentiality rule prohibiting employees from discussing sexual harassment complaints among themselves. The National Labor Relations Board found no justification for the rule and concluded it interfered with the employees' right to engage in "concerted activity." The NLRB said this case was different from its earlier decision upholding an employer's confidentiality rule regarding an ongoing drug investigation. In the earlier case the rule was legitimately designed to protect witnesses and preserve evidence; there was no similar justification here.

Pro-union screen-savers. A hospital allowed its nurses to display personalized screen-saver messages on their computers, but when one nurse posted the message "Look for the U" during a union organizing campaign, the hospital disciplined her. The NLRB said the hospital committed an unfair labor practice in doing so. The hospital's reliance on an earlier bulletin board case was misplaced, said the NLRB, because all that case said was that employees have no absolute right to use company bulletin boards. However, when the employer allows employees to use bulletin boards (or computer monitors) for *some* non-work purposes, the employer can't then discriminate against union-related notices.

Distribution of literature. In another hospital case, a nurse's union initiated a "safe care" campaign addressing the adverse effect on patients caused by downsizing and restructuring the nursing staff and hiring non-professional employees. The campaign included distribution of literature that, according to the hospital, was "shocking and sensational" and that would upset patients. The court recognized that while the hospital was generally allowed to prohibit the distribution of literature by on-duty nurses in work areas, the nurses in this case

were off-duty and they were distributing only to other nurses in a way that did not interfere with patient care. Therefore, the distribution was protected activity.

Law suits. The National Labor Relations Act prohibits employers from restraining, coercing, or interfering with employees' exercise of rights related to self-organization, collective bargaining, and other concerted activity. On the other hand, the First Amendment to the Constitution grants everyone the right to "petition the Government for a redress of grievances" – a right the Supreme Court has characterized as one of our most precious liberties. This right to petition includes the right to sue in court So while an employer's lawsuit against a union *can in theory* amount to illegal interference, the lawsuit would have to be an objectively baseless sham, intended to be abusive, in order to hold an employer liable. Just because the employer loses a suit against its union does not mean the employer acted illegally.

Threats. Unions can commit unfair labor practices, too. When union organizers threatened to retaliate against rank-and-file employees should the union not win the election, the election itself was tainted and the company did not need to recognize the union for bargaining purposes.

Statutory reference. 29 U.S.C. § 151.

Case references. *Phoenix Transit System*, 337 NLRB No. 78 (2002); *Caesar's Palace*, 336 NLRB No. 19 (2001); *St. Joseph's Hospital*, 337 NLRB No. 12 (2001); *Honeywell, Inc.* 262 NLRB 1402 (1982); *Brockton Hospital v. NLRB*, ___F.3d___, 2002 WL 1393571 (D.C.Cir. 2002); *BE&K Construction Co. v. NLRB*, 122 S.Ct. 2390 (2002); *NLRB v. Kentucky Tennessee Clay Co.*, ___F.3d___, 2002 WL 1485145 (4th Cir. 2002).

Project Labor Agreements and the Woodrow Wilson Bridge

A Project Labor Agreement, or PLA, is a multi-employer pre-hire agreement designed to systemize labor relations at a construction site. Typically, PLA's require all contractors and subcontractors who will work on a project to agree in advance to a "master" collective bargaining agreement under which wages, hours and other conditions of employment are standardized for all employees at the project. The PLA requirement is incorporated into bid specifications, so any company that is awarded a contract is bound to join in the PLA.

The National Labor Relations Act expressly permits employers in the building and construction industry to enter into PLA's with a union, even though the union has not yet been established as the representative of a majority of the employees to be covered by the PLA.

The Building and Construction Trades Department (BCTD) of the AFL-CIO negotiated just such an agreement in connection with replacement of the Woodrow Wilson Bridge. The bridge, originally owned by the federal government, was transferred to an interstate authority created by the District of Columbia, Maryland and Virginia. Much of the cost, however, remained federal.

Maryland's responsibility was to build the structures crossing the Potomac, as well as highways and interchanges on the Maryland side. An agreement between the BCTD and the Maryland State Highway Administration provided that Maryland would incorporate a PLA into its bid specifications and that the successful bidder would be bound by the PLA regardless of whether the contractor's employees were union members.

In February 2001, President Bush issued Executive Order 13202 providing that, for federally funded construction projects, the government contracting authority can neither require, nor prohibit, PLA's. As a

result, it would be up to each contractor working on a project to decide whether to enter into, and to require its subcontractors to enter into, a PLA for that project.

When Maryland submitted its proposed bid specifications to the Federal Highway Administration for approval, the FHWA rejected them because, contrary to EO 13202, the bid specs required adherence to a PLA. Maryland then revised its specs to eliminate any PLA requirement.

Maryland's resulting contract award left the BCTD no role to play in the project. So BCTD, among other plaintiffs, sued to invalidate EO 13202 on the theory that the Executive Order went beyond the President's authority and was inconsistent with federal labor law.

The U.S. Court of Appeals for the D.C. Circuit rejected the BCTD's arguments. The Court said that in projects such as the Wilson Bridge, the government is spending its own money. By prescribing how that money is to be spent, the President is simply supervising the Executive Branch, not making laws or issuing regulations that require Congressional authority.

Nor does the Executive Order conflict with the National Labor Relations Act. While that Act *permits* employers to enter into PLA's without violating federal law, nothing in the Act *requires* employers to do so or f*orbids* them from refusing to do so. So the federal government, as proprietor of its own funds, enjoys the same freedom as any other employer to accept or reject a PLA.

Statutory reference. 29 U.S.C. § 158.

Regulatory reference. EO 13202.

Case reference. *Building & Construction Trades Dept. v. Allbaugh*, ___F.3d___, 2002 WL 1484942 (D.C.Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 19.08.

Employee Who Quits Because Boss Can't May Be Entitled to UI Benefits

If an employee voluntarily quits, he is normally not entitled to unemployment insurance (UI) benefits. But if an employee quits for a good cause, he will not be disqualified from receiving benefits. See "Quitting to Take Better Job Not 'Good Cause' for UI Benefit Purposes," *Employer Alerts!*, July 2002, p. 4.

What if an employee quits because her boss is a smoker and she can't stand to be around second-hand cigarette smoke – does that constitute good cause?

Karen Branson was hired as an attorney at Cooper and Associates by Algernon Cooper. After five months on the job, she quit because she was continually exposed to cigarette smoke from Cooper's office.

After leaving Cooper and Associates, she filed a claim for UI benefits with the D.C. Department of Employment Services (DOES). Acknowledging that her termination was voluntary, she argued that she left for good cause. She based her argument on D.C. regulations that define "good cause" to include (1) an illness or disability caused or aggravated by work , and (2) unsafe working conditions.

The Court rejected Branson's illness-or-disability argument because she failed to present any medical evidence, either at time of hire or thereafter, that she was allergic to smoke. As the Court said –

> An employee who claims to have resigned for medical reasons must provide the employer with a medical statement before resigning so that the employer can verify the condition and make an accommodation if necessary.

The Court agreed, however, with Branson's unsafe-working-conditions argument. The Court therefore sent the case back to DOES for further consideration.

Statutory reference. D.C. Code § 51-110.

Regulatory reference. 7 DCMR § 311.

Case reference. *Branson v. DOES*, ___A.2d___ (D.C. No. 99-AA-115, decided June 27, 2002).

EMPLOYER'S SURVIVAL GUIDE reference. 8.03.

D.C. Enacts "Little COBRA" Law

Under the federal law known as COBRA, employers with 20 or more employees who sponsor group medical expense insurance coverage are required to provide continuing coverage in situations where insurance would otherwise terminate. The District of Columbia now joins a number of other jurisdictions that require similar continuation coverage for employers who do not meet the 20-employee COBRA threshold.

Sometimes referred to as "little COBRA" laws, these state enactments often differ from COBRA in terms of notice provisions, coverage requirements and cost-shifting. The new D.C. law, for example, covers all employers whose employees are not otherwise eligible for COBRA benefits. Under the D.C. law, coverage extends for three months (as compared with COBRA continuation coverage of 18 months or 36 months, depending on the circumstances).

D.C.'s new permanent law took effect on June 25, 2002, following temporary emergency legislation. Maryland has had a little COBRA law on its books for a number of years.

Statutory references. D.C. Code § 32-731; Md. Code, Ins. § 15-407.

***EMPLOYER'S SURVIVAL GUIDE* reference.** 9.04.

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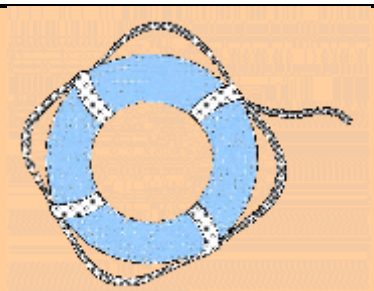

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By Charles H. Fleischer, Esq.

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"Reverse" Age Discrimination Violates ADEA

The federal Age Discrimination in Employment Act (ADEA) protects workers who are 40 years of age and older. So promoting a 45-year-old over a 55-year-old based on age considerations is illegal under federal law. (Unlike federal law, state and local age discrimination laws often have no age threshold.)

But what if the boss *prefers* the older worker? Does the younger one have a claim?

General Dynamics Land Systems had a collective bargaining agreement with one of its labor unions that obligated it to provide full health benefits to retirees who had accumulated 30 years of seniority. When the company negotiated a new collective bargaining agreement, it obtained union approval to delete the health benefit requirement for retirees. However, under the new agreement, employees who were then 50 years of age were "grandfathered" – they still got full benefits when they retired.

After the new collective bargaining agreement was finalized, a group of General Dynamics workers who were between 40 and 49 years old brought a class action against the company, claiming age discrimination. The company acknowledged that while the new agreement appeared on its face to discriminate by creating two classes of employees based solely on age, nevertheless there was no discrimination here. That was so, claimed the company, because the ADEA was intended to protect *older* workers, not those who suffer age discrimination because they are too *young*.

The U.S. Court of Appeals for the Sixth Circuit (which hears federal appeals from Kentucky, Michigan, Ohio and Tennessee) found there *was* discrimination.

In this issue ...

Noting that a number of other federal courts have rejected so-called "reverse" discrimination claims under the ADEA, the Court nevertheless concluded that the ADEA's plain language applies to all persons 40 years or older. The Court also pointed out that its decision is consistent with EEOC regulations, which say –

> It is unlawful ... for an employer to discriminate in hiring or in any other way by giving preference because of age between individuals 40 and over. Thus, if two people apply for the same position, and one is 42 and the other is 52, the employer may not lawfully turn down either one on the basis of age, but must make such decision on the basis of some other factor.

Since the lower courts are in disagreement on the issue, it is a good candidate for Supreme Court resolution. In the meantime, employers would do well to disregard age when it comes to employers 40 and over, even if the age factor might favor the older worker.

Statutory reference. 29 U.S.C. § 621.

Regulatory reference. 29 C.F.R. § 1625.

Case reference. *Cline v. General Dynamics Land Systems, Inc*., 296 F.3d 466 (6th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.02.

Does Murder After Failed Office Romance "Arise Out of" Employment?

Chris Blake killed his co-worker and former girlfriend, Achara Tanatchangsang, at their employer's factory in Portland, Oregon. Prior to the killing, they had worked the same shift and had become romantically involved. When Achara ended the relationship, Blake told his supervisor that he was having difficulty coping with the breakup. After a few months, Blake took medical leave. While still on leave, he entered the plant during normal working hours, shot and killed Achara, and then killed himself.

Achara's estate sued the employer on a civil cause of action known as wrongful death, claiming the employer was negligent in failing to provide sufficient workplace security. The employer denied negligence, but it also responded that even if it were negligent, Oregon's worker's compensation law provided the exclusive remedy and barred a wrongful death suit.

The Oregon statute, like most state's workers' comp laws, covers injuries that "arise out of and in the course of employment." Here it was undisputed that Achara's death arose "in the course of" her employment, since it happened while she was working at her employer's plant. So the only question before the Oregon Supreme Court was whether the death also arose "out of" her employment.

The Court began its analysis by citing earlier decisions for the proposition that

> risks [of injury] distinctly associated with the employment are universally compensable [that is, *covered* by the workers' comp statute]; risks personal to the claimant are universally noncompensable; and neutral risks are compensable if the conditions of employment put the claimant in a position to be injured.

The shooting in this case, according to the Court, was not associated with Achara's employment. Instead, it arose from her and Blake's private life. Achara's decision to end the relationship and Blake's difficulty in coping with that decision were not workplace events but personal matters. Therefore, Achara's death did not arise out of employment and the workers' comp statute was not a bar to her estate's wrongful death action.

Although Oregon's workers' comp statute is similar to the comp statutes in the three local jurisdictions, differences in statutory language and court interpretations may yield different results.

Maryland

Two cases in Maryland involved firearm assaults against employees. Unlike the Oregon case, however, the shooters in Maryland were not employees – in one of the cases, the shooter was an estranged paramour, and in the other case he was a jealous husband who mistakenly thought the victim was having an affair with his wife. In both cases, the Maryland Court of Appeals said the shootings were covered by that state's workers' compensation law.

The Court relied on a unique aspect of Maryland law that provides coverage for the "wilful or negligent act of a third person [a non-employee] directed against an employee in the course of his employment" without also requiring that the act arise "out of" the employment. It is not clear from these cases how the Maryland courts would rule if the shooter had been a co-employee instead of a "third person" or if the shooting had grown out of a voluntary, after-hours relationship.

Virginia

Virginia seems to take an approach similar to Oregon. In a series of cases involving sexual assaults against employees, either by co-employees or third persons, the courts there have taken the view that if the assault was not directed against the employee *because* she was an employee, then the assault does not arise out of employment. In other words, the risk of being sexually assaulted (and, presumably, shot after a failed romance), is normally a personal risk unrelated to employment.

On the other hand, if job requirements place an employee at greater risk of assault, or if the employee is assaulted because of her job, her resultant injuries will be covered by workers' comp.

The distinction isn't always easy to make. Take, for example, the Virginia Supreme Court case of a pressroom employee for a newspaper company who was repeatedly "goosed" by his supervisor. (The Court felt it necessary to define the term "goose," as "to poke or dig a person in some sensitive spot ... especially between the buttocks with an upward thrust of a finger or hand from the rear.") These incidents caused the pressman to suffer depression and post-traumatic stress disorder.

In response to the pressman's suit for injuries, the newspaper company raised Virginia's workers' comp statute as a bar. The newspaper company offered evidence that goosing was prevalent in its pressroom, that it had been for more than forty years, and that it was prevalent in pressrooms elsewhere in the country. The Court rejected this argument, saying that the offending conduct was personal and did not arise out of employment. According to the Court, the "gooser" considered the "goosee" his friend and considered goosing an act of friendship. Go figure.

District of Columbia

It is not clear from the cases just how the D.C. courts would resolve the issue of an intentional assault by another employee. In an early case, a supervisor and his employee had been engaged in "friendly" banter for a number of months, including the use of less-than-complimentary nicknames for each other. On one particular occasion, this banter got out of hand and the supervisor punched and injured the other employee.

The Court found the employee's injuries compensable, pointing out that banter, horseplay and the risk of injury that sometimes follows, are part of the workplace. The Court mentioned that there was no private or personal relationship between the supervisor and the employee outside the workplace.

In a more recent case, Janet Clark, an employee at a D.C. health clinic, parked her car in her employer's lot and reported to work. Later that day, an unidentified man inquired about the car and, when Clark went to the

parking lot and identified the car as hers, the man shot her and fled. The identity of the shooter was never discovered, nor was his motive for the shooting.

Recognizing that, to be compensable an injury must both arise out of and occur in the course of employment, the D.C. Court of Appeals nevertheless ruled that Clark's injuries were covered by workers' comp. In doing so, it relied on what it called the "positional-risk test" –

> Pursuant to the positional-risk test, an injury arises out of employment so long as it would not have happened but for the fact that conditions and obligations of the employment placed the claimant in a position where he was injured. ... This theory supports compensation, for example, in cases of stray bullets, roving lunatics, and other situations in which the only connection of the employment with the injury is that its obligations placed the employee in the particular place at the particular time when he or she was injured.

On the other hand, even under the positional-risk test, injuries resulting from risks that are personal to the claimant and to which the employment contributes nothing are not covered. Just how this test would apply in the case of an ex-lover/co-employee's assault is unclear.

* * * * *

Aside from workers' comp considerations, employers have an obligation to provide a safe workplace for their employees, including protection from workplace violence. Taking the following steps will go a long way to satisfying that obligation –

- **!** Adopt, disseminate and enforce a policy that any violence or threats of violence by employees will be met with dismissal.
- **!** Be alert to any history of violence in applicants for employment.
- **!** When an employee is involved in a domestic situation, take his or her concerns about violence seriously.
- **!** Prohibit employees from bringing weapons of any kind to the employer's place of business or from carrying weapons during working hours. (This rule should apply even where state law allows the carrying of weapons.)
- **!** Prohibit employee use or possession of alcohol and illegal drugs, or being under the influence of alcohol or drugs, while on the job.
- **!** Prohibit, or at least control, horseplay, teasing and the like. (Activities like these can amount to harassment and, if focused on gender, race, age, etc., constitute illegal discrimination.)
- **!** For larger employers, require photo ID badges for all employees.
- **!** Secure non-public work areas and limit access to persons with keys or passcards.
- **!** Secure *all* areas after normal working hours.
- **!** Provide adequate lighting and surveillance for storage and garage areas.
- **!** Provide cell phones to employees who work off-premises.
- **!** Restrict distribution of employee directories, particularly if they contain home addresses, home telephone numbers, names of spouse or children, or other personal information.

Case references. *Panpat v. Owens-Brockway Glass Container, Inc.*, 49 P.3d 773 (Or. 2002); *Edgewood Nursing Home v. Maxwell*, 384 A.2d 748 (Md. 1978); *Giant Food, Inc. v. Gooch*, 225 A.2d 431 (Md. 1967); *Morgan v. MDC Holdings, Inc.*, 2000 WL 1210879 (Vir. Cir. 2000); *Carr v. City of Norfolk*, 422 S.E.2d

417 (Va.App. 1992); *Richmond Newspapers, Inc. v. Hazelwood*, 457 S.E.2d 56 (Va. 1995); *Hartford Accident & Indem. Co. v. Cardillo*, 112 F.2d 11 (D.C.Cir. 1940); *Clark v. District of Columbia Dept. of Employment Services*, 743 A.2d 722 (D.C. 2000).

***EMPLOYER'S SURVIVAL GUIDE* references.** 7.02; 10.08.

Limiting Heart Patient's Overtime Not Required by ADA

To be "disabled" under the Americans with Disabilities Act, an employee must have a physical or mental impairment that substantially limits one or more major life activities. "Major life activities" include caring for oneself, walking, seeing, hearing, and performing manual tasks. See "Supreme Court Limits Disability Discrimination Claims," *Employer Alerts!* (Feb. 2002), p. 1.

EEOC regulations include "working" as a major life activity. However, the Supreme Court has questioned (without yet clearly deciding) whether "working" qualifies. It is somewhat illogical, for example, to conclude that a person is disabled under the ADA because he is unable to work and at the same time conclude that he qualifies for ADA protection because, with or without reasonable accommodation, he is able to perform the essential functions of his job. Even under EEOC regs, however, the inability to perform a specific job does not constitute a substantial limitation in the major life activity of working; instead, the person must be unable to perform a broad range of jobs.

If working does qualify as a major life activity for ADA disability purposes, is an employee disabled because he can work an eight-hour shift, but can't work overtime?

In a recent case before the U.S. District Court for Maryland, the chief of Anne Arundel Medical Center's Ultrasound unit suffered from severe coronary artery disease. After recuperating from a heart attack, he asked that for medical reasons he be relieved from all overtime duties – duties that had been an important part of his job in the past and that were expressly included in his job description. The Medical Center refused the request, insisting that he work overtime as needed. When he refused, the medical center disciplined him. That in turn led to an ADA lawsuit.

The Court *assumed* for purposes of its decision (without necessarily concluding) that working is a major life activity under the ADA. Nevertheless, the Court ruled that the employee's mere inability to work overtime, as required by this particular job, did not mean that he was substantially limited in his ability to work generally at a broad range of jobs. Therefore, the employee was not "disabled" within the meaning of the ADA and the medical center had no duty to accommodate him by limiting his overtime.

Statutory reference. 42 U.S.C. § 12102.

Regulatory reference. 29 C.F.R.§ 1630.

Case reference. *Parkinson v. Anne Arundel Medical Center, Inc.*, ___F.Supp.2d___, 2002 WL 1805659 (D.Md. 2002); *Murphy v. United Parcel Service, Inc.*, 527 U.S. 516 (1999).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.03.

Employer May Cancel COBRA Coverage for Nonpayment of Premiums

Employers with group health insurance plans who have 20 or more employees must offer continuation benefits to plan participants after a "qualifying event" that would otherwise cause loss of coverage. This requirement is was added to the Employee Retirement Income Security Act in 1986 by

legislation with the imposing name "Consolidated Omnibus Budget Reconciliation Act." Hence the continuing coverage requirement is known as "COBRA".

"Qualifying events" include –

- an employee voluntarily quitting;
- an employee being fired (except in cases of gross misconduct);
- an employee becoming ineligible for coverage because of a reduction in hours of work;
- an employee dying and leaving a covered spouse or dependent;
- a covered spouse becoming divorced or separated; and
- a covered dependent ceasing to be a dependent, such as by reaching the policy's age limit.

The employer does not, of course, have to pay for continuing coverage. In fact, the former employee, spouse or dependent not only pays the premium, he or she can also be required to pay an additional 2% to offset the employer's administrative costs in continuing the coverage.

But what if the former employer fails to pay, pays late, or simply doesn't have the money?

William Butler worked for Reid Metal Erectors in Mississippi and was covered by that company's group health insurance plan. When Butler learned he had cancer, he immediately quit his job. The company then notified Butler that he had 60 days to elect COBRA continuation coverage, but Butler responded that he had no income and was unable to pay the premiums.

Later, Butler sued for policy benefits and the case ended up in federal court. The court, citing COBRA's statutory provisions, said that group health plans have the right to require payment for continuation coverage. Under the statute, COBRA rights end on "the date on which coverage ceases under the plan by reason of failure to make timely payment of any premium." In other words, those seeking COBRA continuation coverage are not entitled to a "free ride."

Statutory reference. 29 U.S.C. § 1161.

Case reference. *Butler v. Trustmark Ins. Co.*, ___F.Supp.2d___, 2002 WL 1498551 (S.D.Miss. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 9.04.

Virginia Rejects Federal Public Policy as Basis for Abusive Discharge Claim

Last July we reported that *federal* public policy would not support an abusive discharge claim in Maryland. See "Red Cross May Fire Employee for Reporting Blood-Handling Violations," *Employer Alerts!* (July 2002), p. 4. A federal court in Virginia has now reached a similar conclusion.

The case involved a company known as Patient First Corporation, which operates ambulatory care facilities in the region. The company employed one Stephen Storey as its vice president and chief financial officer. According to Storey, the company improperly billed the federal government for some $500,000 in medical services provided to CHAMPUS beneficiaries. The improper billings arose, said Storey, because of the company's practice of using active-duty miliary doctors who moonlighted for the company.

Concerned that the company (and he as its CFO) might face substantial liability, Story reported these improper billing to senior management. The company's response was to make some changes in its billing practices which reduced, but did not eliminate, the

problem. The company refused to repay amounts already improperly billed and, according to Storey, it altered the records it submitted to CHAMPUS to cover up its billing practices.

Storey then brought his concerns to the company's board of directors. Initially, the board responded by engaging outside counsel to investigate. According to Storey, however, before counsel could submit a report the board terminated counsel's engagement and it secretly voted to fire Storey. So Storey sued, claiming his firing was illegal on a number of grounds.

One of Storey's grounds was the abusive discharge exception to the employment-at-will doctrine. Under that exception, an employee-at-will, who can generally be fired for any reason or for no reason, can sue for wrongful discharge if he was fired in violation of some important public policy. See "Wrongful Termination Update," *Employer Alerts!* (Oct. 2001), p. 1. Here, Storey said his discharge was contrary to *federal* public policy, since the federal government was allegedly being overbilled for medical services.

The Court rejected this theory, pointing out that in Virginia, an abusive discharge claim must identify a *Virginia* statute that the employer violated in terminating the employee. Public policy cannot be rooted in an act of Congress.

Patient First Corporation was not off the hook, however, since Storey's suit was also based on the anti-retaliation provision of the federal False Claims Act. That Act allows private individuals to report fraud by government contractors and to initiate suits against government contractors in the name of the government. The Act goes on to say –

> Any employee who is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by his or her employer because of lawful acts done ... in furtherance of an action under this section ... shall be entitled to all relief necessary to make the employee whole.

The remedies potentially available to Storey under the False Claims Act include reinstatement to his former position, double damages for the pay he lost, and reimbursement for Storey's attorney fees.

Virginia has its own version of the False Claims Act. for fraud against the Commonwealth. See "Virginia's New Whistleblower Law," *Employer Alerts!* (June 2002), p. 9.

Case reference. *Storey v. Patient First Corp.*, ___F.Supp.2d___, 2002 WL 1331857 (E.D.Va. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.03

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By Charles H. Fleischer, Esq.

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Sarbanes-Oxley Act's Employment-Related Provisions

The rash of recent corporate scandals by publicly traded companies has prompted Congress to pass tough new legislation. Although the Sarbanes-Oxley Act of 2002 focuses primarily on accounting oversight and corporate governance, the Act contains a number of provisions that directly affect high-level, and in some cases lower echelon, employees of publicly-traded companies.

Certification of financial statements. The Act requires the SEC to issue rules requiring a company's principal executive and financial officers to certify the company's financial statements as true and complete. In the event of any failure to comply with reporting requirements such that financial statements have to be restated, those same officers must forfeit their bonuses and incentive compensation for a 12-month period.

Blackouts. Whenever a company imposes a blackout by prohibiting pension plan participants from trading in company stock, company directors and executive officers are also prohibited from selling any stock they may have acquired through their employment with the company. Plan administrators must give advance notice of the blackout to plan participants and beneficiaries, including the reason for the blackout.

Loans. Subject to certain narrow exceptions, companies are now prohibited from making personal loans or extending credit to their directors and executive officers.

Code of Ethics. Companies must report to the SEC

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whether they have adopted a code of ethics for their senior financial officers and, if they haven't, why they haven't.

Document retention. Pursuant to the Act, the SEC will adopt rules governing companies' retention of documents relating to financial audits and reviews. Knowing and willful violation of the rules will be a criminal offense.

Fitness to serve. The SEC is authorized by the Act to prohibit persons who are deemed unfit from serving as officers or directors if they have violated rules governing deception or fraud.

Whistleblowing. It will also now be criminal for a company to retaliate against an employee who assists in any investigation by federal regulators, Congress, or company supervisors or who provides information to federal law enforcement officers. Any person who suffers unlawful retaliation may also initiate a civil proceeding for reinstatement, backpay and other damages.

Statutory reference. Sarbanes-Oxley Act of 2002, Pub.L. 107-204.

***EMPLOYER'S SURVIVAL GUIDE* references.** 1.03, 19.05.

OSHA Announces Draft Ergonomics Guidelines for Nursing Homes

Ergonomics – the study of the relationship between workers and their work environment – has long been a controversial topic. As the Clinton administration drew to a close, the U.S. Department of Labor's Occupational Safety and Health Administration issued a comprehensive, broadly applicable regulation covering musculo-skeletal disorders, or MSD's, caused by exposure to risk factors over a period of time. See "OSHA's New Ergonomic Standards," *Employer Alerts!* (Dec. 2002), p. 2. Before those regulations became operative, however, Congress passed a joint resolution of disapproval, which repealed the regulations. See "Ergonomics Regulations Repealed," *Employer Alerts!* (April 2001), p. 8.

Despite Congressional repeal, OSHA never abandoned the field and has been studying ergonomics ever since. As part of that process, it announced in April of this year a protocol for developing industry- and task-specific guidelines. It then announced that nursing homes would be the first industry for which guidelines would be issued.

OSHA has now issued those guidelines in draft form for comment. The nursing home guidelines, along with additional ergonomics information, are available at http://www.osha.gov/ergonomics/. Grocery stores and poultry processing will be the focus of the next two sets of industry-specific guidelines, according to OSHA.

Although the guidelines are non-binding, in the sense that OSHA will not rely on them for enforcement purposes, employers still have a duty under the "general duty" clause of the Occupational Safety and Health Act to provide a safe workplace. Despite their non-binding status, the guidelines could conceivably be used to show that an employer has violated the general duty clause.

Statutory reference. 29 U.S.C. § 651.

Regulatory reference. 67 Fed.Reg. 55884 (Aug. 30, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 10.07.

Consumer-Directed Health Plans: FSA's and HRA's

Health maintenance organizations (HMO's) and preferred provider organizations (PPO's) may help curb runaway inflation in health care costs, but they have some undesirable features. For example,

participating employees are usually limited to a panel of health care providers chosen by the insurance company and they must go to their gatekeeper physicians before seeing specialists. If they go out of network, their expenses may not be covered at all, or they may be covered at substantially reduced rates.

Under a consumer-directed health plan, the employee may choose any health care provider he wishes, go as often or as infrequently as he likes, and (so long as the expenses would qualify for an income tax deduction) obtain reimbursement for all his expense. Two types of plans that give consumers a bit more choice – Flexible Spending Arrangements (FSA's) and Health Reimbursement Arrangements (HRA's) – are becoming increasingly popular adjuncts to more traditional insured plans.

FSA's

An FSA is one of the "qualified benefits" an employer may offer as part of a cafeteria plan (also called a section 125 plan). Under a cafeteria plan, the employee chooses between cash and one or more qualified benefits. If an employee chooses cash, he is taxed on the cash at ordinary income rates. Qualified benefits, on the other hand, are not taxable. "Qualified benefits" include health and accident insurance, life insurance, and dependent care benefits, as well as FSA's, all subject to various restrictions and limitations imposed by the Internal Revenue Code.

Assuming the employer offers a medical FSA as part of his cafeteria plan, each employee estimates the amount of uninsured medical expenses he and his family are likely to incur in a particular plan year. These may be in the form of out-of-network charges, deductible or co-insurance obligations, or vision, dental or other medical expenses not covered at all by any existing insurance policy. (FSA's may also be used for dependent care expenses, or for both medical and dependent care expenses.) The employee authorizes his employer to apply some portion of his cafeteria plan benefit to an FSA. Then, as the employee incurs uninsured medical expenses, he submits substantiation of the expense (in the form of bills from health care providers) and is reimbursed for the expenses.

As with other qualified benefits under a cafeteria plan, FSA benefits are not includible in the employee's income, even though the employer may take a deduction just as if the amount had been paid in cash. The net affect is that the employee can pay uninsured medical expenses with *pre-tax* dollars instead of after-tax dollars. While the employee could obtain a similar tax benefit without an FSA, by deducting uninsured medical expenses on his tax return, medical expense deductions are only available to employees who itemize, and they are limited to expenses that exceed 7½% of the employee's adjusted gross income.

The downside of an FSA for employees is that any money left in their FSA accounts at the end of a plan year is forfeited to the employer – a use-it-or-lose-it rule. For that reason, employees should be conservative in their estimates of uninsured medical expenses.

FSA's have a downside for employers, too. Suppose an employee decides that he is likely to incur at least $2,000 in uninsured medical expenses in a particular year, so he elects a $2,000 FSA benefit. Typically, the employer does not fund that $2,000 at the beginning of the plan year. Instead, the employer funds it in increments, as part of his periodic payroll obligations, along with any other benefits that are part of the cafeteria plan. In other words, the full $2,000 isn't actually in the account until the end of the plan year.

But suppose an employee incurs substantial medical expenses early in the plan year and promptly submits reimbursement requests. The employer is required to cover the reimbursements up to the full $2,000 FSA benefit, even though that amount has not yet been deposited. Worse, if the employee then quits, he no longer participates in the cafeteria plan, so in effect the employer cannot recover the $2,000 out of future cafeteria benefits that would have accrued had the employee not quit. To guard against this possibility, cafeteria plans usually place limits on the amount an

employee may elect as an FSA benefit.

HRA's

Although HRA's may look similar to FSA's, in that they reimburse employees for uninsured medical expenses, they are in fact significantly different. For example, unused benefits may be carried over from year to year, instead of being forfeited. In addition, reimbursements are limited to the amount actually accumulated in the account at any given time, so that employers do not risk having to advance benefits early in a plan year that cannot be recovered if the employee quits.

An HRA is typically used in conjunction with a group health insurance policy that has a high deductible amount. Premiums on the group policy, which are low because of the high deductible, can be paid by the employer, the employee, or partly by both, as specified in plan documents. The employer then establishes an additional plan (the HRA) to reimburse employees for uninsured medical expenses. The reimbursement amount usually approximates the amount of the deductible under the group policy, so that employees end up paying little or no medical expenses out of their own pockets. Reimbursement amounts may even be used to purchase health insurance.

HRA plans *may* permit former employees and retirees to have continuing access to unused reimbursement amounts. Since HRA's are subject to COBRA, HRA plans *must* permit former employee who elect COBRA to have access to unused reimbursement amounts.

As with FSA's, HRA's enjoy favorable tax treatment: benefits are deductible by the employer but excludible from the employee's gross income. To qualify for that tax treatment, however, HRA's must –

- be paid for solely by the employer and cannot be funded pursuant to a salary reduction arrangement or cafeteria plan;
- limit reimbursements to *substantiated* (documented) medical expenses incurred while the plan is in existence and while the employee is participating in the plan;
- limit reimbursements to medical expenses that would qualify for deduction as medical expenses for the employee or the employee's spouse and dependents; and
- comply generally with ERISA (including COBRA) and HIPAA.

Statutory reference. 26 U.S.C. § 213.

Regulatory reference. Rev.Rul. 2002-41; IRS Notice 2002-45.

***EMPLOYER'S SURVIVAL GUIDE* references.** 9.04; 9.05.

Are Professional Athletes Covered by Workers' Comp?

Workers' compensation statutes cover accidental work-related injuries. "Accidental" in this context means that the injury must be unintended from the employee's point-of-view. But in professional sports – particularly contact sports like football and hockey, injuries are hardly unusual. As Pro-Football, Inc. (more familiarly known as the Washington Redskins) put it in one case, injuries are "customary," "foreseeable," and "expected."

Does the high likelihood of injuries in professional sports mean that the injuries are not "accidental" and therefore not covered by comp statutes? The rule in almost all cases is that sports injuries *are* covered. A recent decision by the Virginia Court of Appeals (Virginia's intermediate appellate court) is illustrative.

Jeffrey Uhlenhake, the Redskins' former center, experienced a number of injuries with other teams before

coming to the Redskins in 1996. In 1993, he had reconstructive ACL surgery to his left knee.

In 1997, after joining the Redskins, he injured his left ankle during a game. In another game later that season he re-injured his left knee. After the end of the 1997 season, Uhlenhake underwent further orthopaedic surgery to his left knee.

Uhlenhake's and other players' injuries prompted the Redskins' then coach, Norv Turner, to complain in a December 1997 interview with the *Washington Post*: "I'd like to get to where we could get five guys in there that could play an entire season." (It is curious that while the team's head coach was complaining about injuries, the club owner was instructing his lawyers to argue that player injuries are so highly likely as to be "automatically" expected.)

Uhlenhake's doctor eventually concluded that he had permanent impairment to his left ankle due to arthritis, and permanent impairment to his left knee from the ACL injuries. So Uhlenhake filed for workers' compensation benefits in Virginia, where his employment relationship with the Redskins had arisen.

The Redskins contested coverage, arguing in effect that injuries like those suffered by Uhlenhake are just part of the game, and therefore not accidental. The Virginia Court of Appeals rejected that argument. The Court held that the degree of risk associated with particular employment has no bearing on whether resultant injuries are compensable. To rule otherwise, said the Court, would be to deny coverage for a whole range of high-risk professions, which is exactly contrary to the purpose of workers' compensation laws.

It should be noted that the Virginia Supreme Court has granted an appeal in Uhlenhake's case. No hearing date has yet been set.

In a more recent Virginia case, the Court of Appeals ruled that Redskin Tito Paul's injuries were covered by Virginia's, not Colorado's comp statute, even thought the contract under which Paul was playing was originally between him and the Denver Broncos. The Court did not even bother to discuss whether Paul's injuries were accidental.

Maryland has one of the few court decisions in which compensation was *denied* to a professional athlete. David Rowe, a 6' 8", 280-pound defensive tackle for the former Baltimore Colts, suffered a serious injury to his right arm during a scrimmage. Rowe's claim for compensation was denied because, said the Court, his injuries were not unusual or unexpected. Instead, said the Court, "risk of injury is an integral part of the game, and possibly accounts for the reason players receive the salaries they are paid."

While Rowe's case was pending, the Maryland legislature amended that state's workers' comp statute to provide that "compensation may not be denied to an employee because of the degree of risk associated with the employment." That amendment effectively overruled the Court's decision against Rowe and brought Maryland in line with the vast majority of other states.

The District of Columbia appears to agree with the majority rule as well. In another case involving the Redskins, fourteen players sued for workers' compensation benefits for injuries sustained "in the course of their often heroic but always perilous employment." The only question in the case was whether the District's or Virginia's workers' comp statute should govern. The Court apparently just assumed that player injuries were fully covered.

Statutory references. Md. Code, L&E § 9-101; Va. Code § 65.2-100; D.C.Code § 32-1501.

Case references. *Pro-Football, Inc. v. Uhlenhake*, 558 S.E.2d 571 (Va.App. 2002), *appeal granted* (Va. No. 020343, June 5, 2002); *Pro-Football, Inc. v. Paul*, 2002 WL 2002708 (Va.App. 2002); *Rowe v. Baltimore Colts*, 454 A.2d 872 (Md.App. 1983); *Pro-Football, Inc. v. DOES*, 588 A.2d 275 (D.C. 1991).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 7.02.

Bordello Wins Title VII Case Thanks to Poor Record-Keeping

Title VII of the federal Civil Rights Act allows victims of employment discrimination to sue their employers, but only if their employers have 15 or more employees for each working day in each of 20 or more calendar weeks in the current or the preceding calendar year.

This threshold requirement helps to insure that the employer is engaged in interstate commerce – a constitutional requirement for some types of federal legislation. The requirement also frees very small employers from having to defend EEOC administrative charges and federal court lawsuits. (State and local discrimination laws often have lower thresholds, so that employees of smaller employers may still be able to pursue their claims.)

The burden of proving the threshold, 15-employee requirement is on the employee claiming discrimination. That is exactly the problem Kerry Stinnett faced when he decided to sue his employer for sexual harassment.

Stinnett worked for Iron Works Gym, an apparently legitimate business owned by Executive Health Spa in Illinois. The Spa – another business located down the street from the Gym – was in turn was owned by Kathy Andrews, Stinnett's boss. Under the guise of offering massages, the Spa was in reality a house of prostitution.

The Gym employed nine persons, including Stinnett. That alone was not an insurmountable problem, because the law permits aggregation of businesses owned in common for purposes of counting employees. The parties in this case both agreed that the Gym and the Spa should be treated as a single entity for headcount purposes. But the problem was proving how many employees the Spa had.

Stinnett tried to offer testimony from one woman who worked at the Spa, and from another woman who was participating in a federal investigation of the Spa. Their knowledge, however, was based on information that in one case was several years before, and in the other case was several years after, Stinnett allegedly suffered discrimination. Stinnett himself was no help, because his boss kept him away from the Spa and his testimony was inconsistent.

The only other evidence was from Kathy Andrews, who, not surprisingly, had limited employment records and characterized her "Spa attendants" as independent contractors. Whether or not that characterization was correct, there still appeared to be no more than 14 total employees in the combined enterprise at any given time.

Having failed to prove that his employer had the requisite 15 employees, Stinnett failed to meet his burden and his case was dismissed.

Statutory reference. 42 U.S.C. § 2000e.

Case reference. *Stinnett v. Iron Works Gym*, 2002 WL 1962138 (7th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.01.

FLSA and Illegal Aliens

Jutla Oil recruited Macan Singh to come work for the company in California. Jutla promised Singh a place to live, tuition for his education, and that Singh would eventually become a partner in the business. Singh, an illegal alien, worked for Jutla from May of 1995 to February of 1998 but received no pay.

In early 1999, Singh filed a claim for unpaid wages. The parties eventually settled the claim, with Jutla

agreeing to make installment payments to Singh. The day after the agreement, the Immigration and Naturalization Service arrested Singh.

Singh sued Jutla under the Fair Labor Standards Act, alleging that Jutla had informed the INS of Singh's illegal status in retaliation for Singh's wage claim. That, claimed Singh, was a violation of the FLSA's anti-retaliation provision, which makes it illegal to

> discharge or in any manner discriminate against any employee because such employee has filed any complaint or instituted or caused to be instituted any proceeding under or related to this Act.

The question before the federal district court in California was whether Singh's status as an illegal alien precluded him from suing under the FLSA.

In addressing that question, the Court first reviewed relevant Supreme Court decisions. Although the Supreme Court has never dealt explicitly with the rights of undocumented workers under the FLSA, it has dealt with similar questions under the National Labor Relations Act. Back in 1984, for example, in a case called *Sure-Tan*, the Supreme Court held that undocumented workers are considered "employees" under federal labor laws and can therefore sue for violations of those laws. However, just this past spring, in *Hoffman Plastics*, the Supreme Court denied an award of backpay to an illegal alien who had been fired for engaging in union organizing activity. See "Supreme Court Update," *Employer Alerts!* (May 2002), p. 1. ("Backpay" in this context means pay that an employee would have earned during the period from being illegally fired up to the time his case is decided in court. See "Salts, Testers and Backpay Awards," *Employer Alerts!* (May 2002), p. 3.)

How to reconcile *Sure-Tan* and *Hoffman Plastics*? The Court concluded that while reporting an illegal alien to the INS is to be generally encouraged, making such a report with a motive to retaliate, as Jutla allegedly did here, is a violation of FLSA. Therefore, even though backpay is precluded as a remedy, an award of pay for work *actually performed* is not.

The Court rejected Jutla's argument that any award would tend to undermine federal immigration policy. The Court reasoned that to allow an employer to pay less than minimum wage to an undocumented worker simply encourages employers to evade immigration laws and hire illegals.

Statutory reference. 29 U.S.C. § 201

Case reference. *Singh v. Jutla & C.D. & R. Oil, Inc.*, 2002 WL 1808589 (N.D.Cal. 2002); *Sure-Tan, Inc. v. NLRB*, 467 U.S. 883 (1984); *Hoffman Plastics Compounds, Inc. v. NLRB*, 122 S.Ct. 1275 (2002).

***EMPLOYER'S SURVIVAL GUIDE* references.** 1.03; 4.01; 15.06.

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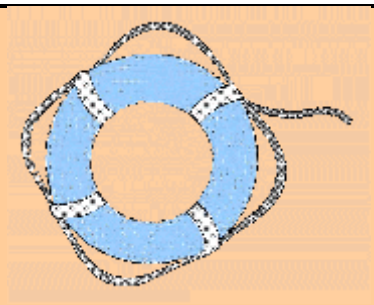

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By Charles H. Fleischer, Esq.

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More on Employee Handbooks

Last August we reported on several D.C. Court of Appeals cases in which employee handbooks were held to be employment contracts. See "Employee Handbooks and Employment Contracts," *Employer Alerts!* (Aug. 2002), p. 1. We went on to recommend a number of steps an employer might take to avoid that unfortunate result. Now another D.C. Court of Appeals case shows that disclaimers and other appropriate provisions in an employee handbook really do help preserve an "at will" employment relationship between an employer and its employees.

Richard Boulton, who worked for the Institute of International Education, claimed that he was fired on account of his sexual orientation and not, as the IIE said, because his position was being eliminated. He also claimed that even if the IIE's reason for the termination were true, his firing would still be invalid because of a provision in the employee handbook. That provision reads –

> Every effort is made to ensure your job security, however, it sometimes becomes necessary to eliminate jobs. If your job is affected, every effort will be made to locate another suitable position for you in IIE. To the extent that it is feasible, on-the-job training in another area of work will be provided for up to a maximum of 30 days.

According to Boulton, IIE was contractually obligated to at least try finding him another suitable position;

In this issue ...

its alleged failure to do so amounted to a breach of its contractual obligation.

The Court of Appeals disagreed. The Court relied on two other provisions of the handbook which said –

> This handbook ... [is] intended to supply you with a basic guide to IIE's policies and procedures which, it should be noted, is not to be considered as creating terms and conditions of an employment contract or a promise of future employment.
>
> The employment relationship that exists between IIE and each of its employees is employment-at-will. Under this relationship, any employee is free to end his or her employment for any reason with or without prior notice. Likewise, IIE may, at its discretion, decide to end an individual's employment.

These two provisions taken together, said the Court, made it clear that an at-will relationship was intended to be preserved.

Significantly, neither provision alone would have been sufficient. In D.C. at least, a handbook that merely states it is not a contract does not necessarily overcome other language that may amount to a promise of employment. The handbook must go on and clearly reserve the employer's right to terminate at will.

Boulton's sexual orientation claim, based on D.C.'s Human Rights Act, was also dismissed for lack of evidence and because it was filed outside the one-year limitation period specified in the Human Rights Act.

Case reference. *Boulton v. Institute of International Education*, __A.2d __ (D.C. No. 01-CV-951, decided Oct. 10, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.05.

Glass Ceiling Is Costly to Silver Spring Employer

StorageTek is a Colorado-based company that manufactures, sells and services storage devices for computer systems. Its Federal Systems Division office, in Silver Spring, Maryland handles StorageTek's federal government contracts. In 1993, StorageTek hired Adrienne Corti as financial services manager (FSM) for Silver Spring office.

Corti's duties as FSM included working with sales reps to structure transactions and respond to federal bid requests. She also negotiated prices and leases. Her compensation consisted of a base salary, plus commissions and bonuses.

By all measures, Corti was an outstanding employee. Her first year on the job she met her sales quota and her second year she ranked first among FSM's in the mid-Atlantic region. She was rewarded with a trip to Hawaii and membership in StorageTek's "Master's Club". Her third year Corti was StorageTek's number one FSM for all the United States and Canada.

The only problem was that Corti needed to work closely with StorageTek's District Sales Manager, Edwin Hartman, and Hartman was not comfortable with a female peer. In Hartman's own words, he was used to having women work *for* him, not *with* him. On various occasions Hartman withheld account information from Corti and failed to inform her about important meetings. And after a company social function, when a number of employees went to play golf, Hartman told Corti and another woman they should go shopping, because golf was a "guy thing." Corti's complaints about Hartman went unheaded.

In late 1995, StorageTek decided to consolidate three of its FSM positions into two, meaning that one of the FSM's would be out of a job. Of the three affected FSM positions, one was Corti's; the other two were held by males whose performances were consistently below

Corti's.

The company in its wisdom decided to eliminate Conti's position, justifying that decision based on negative performance evaluations of Corti. Hartman was partly responsible for those evaluations.

So Corti sued, claiming gender discrimination in violation of Title VII of the federal Civil Rights Act. Her evidence at trial demonstrated that she was a top producer for StorageTek and that she consistently outperformed the two male FSM's who retained their positions. Her evidence also demonstrated that the asserted basis for the company's decision was a mere pretext, and that the real reason was gender.

The federal trial court in Baltimore awarded Corti nothing for so-called compensatory damages (pain and suffering, emotional distress, etc.), but awarded her $410,974 in backpay and $100,000 in punitive damages.

The U.S. Court of Appeals for the Fourth Circuit affirmed the award in all respects. While punitive damages, said the Court, are usually not permitted in the absence of compensatory damages, a backpay award in a Title VII discrimination case is sufficient to support punitive damages.

Case reference. *Corti v. Storage Technology Corp*., 304 F.3d 336 (4th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.01.

Non-Discriminatory Sexual Harassment

The problem with treating sexual harassment as a form of sex discrimination under Title VII is that it's difficult to tell whether the harassment is "because of sex." The problem arises because the term "sex" is both a synonym for "gender" and it is also an instrument of discrimination. When we say that someone is sexually harassing another, do we mean that the harasser's improper conduct is motivated by the victim's gender? Or we mean that the harasser is using sex-laden language or conduct to harass?

The first type of conduct – adverse conduct motived by gender – constitutes illegal discrimination. The second type – talking or acting in a sexually explicit manner – may or may not be illegal.

A number of cases have wrestled with this issue, none very successfully. The Supreme Court recognized the problem in a 1998 case involving male employee "roustabouts" on an oil drilling platform in the Gulf of Mexico. One particular employee was singled out for severe harassment by the others, which took the form of sexually explicit words and conduct, including even threats of rape. Observing that workplace harassment is not "automatically discriminatory merely because the words used have sexual content or connotations," the Court nevertheless concluded that the harassment in that case was discriminatory. The decision is surprising in one sense: there was no discussion whether female employees were or would have been treated differently from the actual victim in the case.

This past January, the U.S. Court of Appeals for the D.C. Circuit concluded, on similar facts, that harassment by fellow security guard employees, though "tinged with offensive sexual connotations," was not based on the victim's sex and was therefore not a Title VII violation. See "When is Harassment Sexual?" *Employer Alerts!* (Feb. 2002), p. 8.

The Fourth Circuit (which hears appeals of federal cases in Maryland and Virginia) has now joined the fray and reached the same conclusion as the D.C. Circuit.

Lisa Ocheltree worked for Scollon Productions in White Rock, South Carolina. Scollon's business is manufacturing costumes for various characters and mascots, such as the South Carolina Gamecock mascot.

Ocheltree, a female, was employed in the primarily male production shop. She testified to numerous incidents of offensive behavior by others during her employment, such as staff engaging openly in discussions about sex, making comments about the sexual behavior of other staff members, using foul, vulgar and profane language, and telling sexually oriented jokes. Other incidents included employees pretending to have sex with mannequins and showing Ocheltree a picture of pierced genitalia.

Ocheltree attempted to speak with company officials about this conduct, but was never given the opportunity. So she brought suit for sexual harassment discrimination. After a trial court jury awarded her $7,280 in compensatory damages and $400,000 in punitive damages, Scollon (Ocheltree's employer) appealed.

The Fourth Circuit began its analysis by pointing out that Title VII "does not prohibit all verbal or physical harassment in the workplace; it is directed only at discrimination because of sex." In other words, "in prohibiting sex discrimination solely on the basis of whether the employee is a man or a woman, Title VII does not reach discrimination based on other reasons, such as the employee's sexual behavior, prudery, or vulnerability."

As to the incidents that Ocheltree complained about, the Court noted that she would have been exposed to the same atmosphere had she been male. The evidence showed that the men's behavior did not begin or change as of the date of Ocheltree's hire, since it had been ongoing before she came to work for Scollon. And while the working environment may have been intimidating, hostile and offensive due to sexually-tinged conduct of male employees, that conduct was not gender-related. The Court therefore reversed the jury's damage award and ruled in Scollon's favor.

In theory, the Court's decision makes eminent good sense. After all, Ocheltree was not singled out for harassment and the conduct she complained about was equally offensive to both men and women. But the decision offers little practical guidance to employers.

Suppose management receives a complaint from a female employee that, because of widespread, pervasive words and conduct of a sexual nature, the workplace environment is intimidating, hostile and offensive. Suppose further that management investigates and finds an obnoxious environment fully justifying the employee's complaint. Would management be on safe ground if it concluded that since the environment was equally offensive to males and females, it need take no action?

Determining the motives of those who are behaving in an offensive manner is not a simple or certain process. And a mistake could expose an employer to hundreds of thousands in damages. So as a practical matter, a prudent employer will attempt to limit sexually-tinged conduct regardless of its motive or its indiscriminate impact.

Statutory reference. 42 U.S.C. § 2000e.

Case references. *Oncale v. Sundowner Offshore Services, Inc.*, 523 U.S. 75 (1998); *Davis v. Coastal Int'l Security, Inc.*, 275 F.3d 1119 (D.C.Cir. 2002); *Ocheltree v. Scollon Productions, Inc.*, 2002 WL 31261098 (4th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.03.

Do Males Suffer Discrimination When Employer Favors Female?

The "because of sex" issue can arise in lots of different contexts. Gerald Schobert and Ronald Werner, for example, who worked for the Illinois Department of Transportation, claimed that Tame Roth, the sole female in the shop, got favorable treatment because she was a woman. According to Schobert and Werner, Roth behaved suggestively around her supervisors. As a result, she was spared from the more difficult and dangerous duty assignments, which fell to Schobert, Werner and other males.

The U.S. Court of Appeals for the Seventh Circuit (which hears federal appeals from Illinois, Indiana and Wisconsin) didn't see it that way. As the Court said –

> Title VII does not ... prevent employers from favoring employees because of personal relationships. Whether the employer grants employment perks to an employee because she is a protegé, an old friend, a close relative or a love interest, that special treatment is permissible as long as it is not based on an impermissible classification.

The Court went on to observe that, from a practical standpoint, "there is every reason for an employer to discourage this kind of intra-office romance ... but that is different from saying that it violates Title VII." Had there been other women in the shop, said the Court, they would have suffered in exactly the same way as Schobert and Werner.

While in a sense the employer may have been biased in Roth's favor "because of sex," it wasn't motivated by gender bias.

Statutory reference. 42. U.S.C. § 2000e.

Case reference. *Schobert v. Illinois Dept. of Transportation*, 304 F.3d 725 (7th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.03.

Disclosure of Trade Secrets May Not Be "Inevitable"

The Uniform Trade Secrets Act, as adopted in Maryland, Virginia and the District of Columbia, permits an employer to go to court for an injunction against a former employee who has misappropriated the employer's trade secrets, or who threatens to do so. See "Trade Secrets and the Inevitable Disclosure Doctrine," *Employer Alerts!* (July 2000), p. 2.

If the former employee has not actually misappropriated trade secrets or threatened to do so, the Uniform Trade Secrets Act doesn't literally apply. However, a number of courts have taken the view that when the former employee has access to highly confidential trade secrets, when the employee's old and new companies are in direct competition, and when the employee's old and new jobs are so similar that disclosure is inevitable, then an injunction will be issued.

A recent California case discussing the doctrine of inevitable disclosure grew out of disputes involving Schlage and Kwikset – two lock manufacturers who are in fierce competition with each other. According to the opinion, they vie intensely for shelf space at Home Depot and other major retailers. Home Depot, for example, alone accounts for 38% of Schlage's sales.

Home Depot periodically conducts a "line review" of its suppliers' product lines, pricing, marketing concessions, and ability to deliver product. Home Depot uses this review to determine which products to carry and which products to drop. As part of this review, Home Depot asks its suppliers, including Schlage and Kwikset, to submit proposals for product lines, pricing, marketing concessions and promotional discounts.

Douglas Whyte worked as Schlage's vice president of sales in California. He signed a confidentiality agreement with Schlage, but not a non-compete agreement. As Schlage's vice president, Whyte was responsible for sales to Home Depot and other retailers, such as Lowe's and Sears. He participated in Home Depot's line review in February 2000 and succeeded in getting Home Depot to remove a particular Kwikset product and expand Schlage's shelf space.

Whyte's accomplishments impressed Kwikset's president, who realized that Whyte was "killing my team." Kwikset approached Whyte and succeeded in hiring him effective June 3, 2000. However, Whyte did not actually resign from Schlage until June 14. In the interim period,

Whyte participated in confidential meetings with Home Depot as Schlage's representative.

Upon departing from Schlage, Whyte became Kwikset's vice president for sales. His job duties there were substantially the same as his former duties at Schlage, including handling sales to Home Depot and other major retailers.

Whyte's departure from Schlage ignited a firestorm of litigation between the two of them. First, Schlage sued Whyte in Colorado, apparently hoping to find a favorable forum there. The Colorado court refused to enjoin Whyte from working for Kwikset. Then Whyte sued Schlage in California and Schlage countersued Whyte in that state.

Based on mixed evidence, the Court in California concluded that while the Schlage information to which Whyte had access did constitute trade secrets, none of Whyte's actions amounted to an actual or threatened disclosure of those secrets. Undeterred, Schlage then argued that Whyte's disclosure of Schlage trade secrets to Kwikset was *inevitable* and that Whyte should therefore be enjoined from selling Kwikset locks to Home Depot. Essentially, Schlage asserted that unless Whyte possessed an "uncanny ability to compartmentalize information," he would necessarily be making decisions about Kwikset's marketing strategy by relying on his knowledge of Schlage's trade secrets.

In addressing Schlage's theory, the Court undertook a thorough review of decisions from other states. The Court concluded that a majority of jurisdictions considering the question have adopted some form of the inevitable disclosure doctrine, although a "small but growing band of cases" reject the doctrine. The Court decided that California should align itself with those jurisdictions that reject the doctrine, and it refused to enjoin Whyte from working for Kwikset.

The Court's basic objection to the doctrine was that it amounts to an after-the-fact non-compete agreement that the employer never bargained for and that the employee never agreed to. The doctrine therefore rewrites the employment arrangement in a way not originally contemplated by the parties.

None of the three local jurisdictions has definitively recognized or rejected the doctrine of inevitable disclosure. A Virginia trial court has said that state does not recognize the doctrine, but the decision is not binding on other Virginia courts. A federal trial court in Maryland has considered the doctrine without ruling whether or not it applies in that state. No District of Columbia court has ruled on the issue.

While the inevitable disclosure doctrine may provide a "last resort" argument for companies facing possible loss of valuable trade secrets, a far better approach is to obtain a clear, written agreement from all employees who have access to critical company data. The agreement should provide that employees will maintain the data in confidence and that after termination of employment they will not solicit the company's customers or engage in competition with the company. And, of course, the agreement should be reasonable in its terms and restrictions.

Case references. *Schlage Lock Co. v. Whyte*, 125 Cal.Rptr.2d 277 (2002); *Padco Advisors, Inc. v. Omdahl* 179 F.Supp.2d 600 (D.Md. 2002); *Government Technology Services, Inc. v. Intellisys Technology Corp.*, 1999 WL 1499548 (Va.Cir. 160265, decided Oct. 20, 1999).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 14.01.

Employer Has No ADA Duty to Create Job for Disabled Employee

Tamara Watson held an assembly line position with Lithonia Lighting, in Crawfordsville, Indiana, for only 10 months before she suffered a shoulder injury. The injury restricted her ability to perform the repetitive motions typical of assembly line work, so

Lithonia assigned her to a temporary position which did not require a full range of motion.

After about a year in the temporary position, Watson was informed by her physician that she would never be able to perform regular assembly line work. Watson then asked Lithonia to accommodate her disability by permanently assigning her to the temporary position. Lithonia refused. According to Lithonia, all its assembly line workers are required to rotate through all positions in order to reduce repetitive motion injuries at any one position. Rotation also assures that everyone is trained on all jobs and available to fill in in emergencies. The temporary position, said Lithonia, was just that – a position it made available to workers recovering from injuries.

Lithonia concluded that it had no available position that Watson could perform, so it terminated her. Watson then sued under the Americans with Disabilities Act, claiming that the company had a duty under the ADA to permanently assign her to the position she temporarily held.

The U.S. Court of Appeals for the Seventh Circuit rejected Watson's claim. It ruled that an employer's duty of reasonable accommodation under the ADA does not require it to create new jobs tailored to each employee's abilities. Lithonia's job rotation requirement serves a legitimate business purpose, and its refusal to allow an employee to permanently hold a temporary, limited duty position was also reasonable.

In fact, said the Court, Lithonia's practice of assigning injured workers to limited duty on a temporary basis is exactly what the ADA encourages. If Lithonia didn't allow limited duty assignments at all, injured workers would lose their jobs. Similarly, if Lithonia filled all its limited duty positions on a permanent basis with disabled employees, workers who later became temporarily unable to rotate through the assembly line would lose their jobs as well.

Statutory reference. 42 U.S.C. § 12101.

Case reference. *Watson v. Lithonia Lighting*, 304 F.3d 749 (7th Cir., 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.03.

Refusal to Work for Safety Reasons Is Protected Concerted Activity

The National Labor Relations Act gives all employees, including non-union employees, the right to engage in "concerted activities for the purpose of ... mutual aid or protection." See "Non-Union Worker's Right to Witness at Disciplinary Hearing," *Employer Alerts!* (Aug. 2000), p. 2; "Labor Law Protections in Non-Union Shops," *Employer Alerts!* (Feb. 2002), p. 6. The National Labor Relations Board has recently ruled that the Act's protections encompass employees' refusal to work under conditions they consider unsafe.

The Odyssey Capital Group owned and managed a 150-unit apartment complex in Pennsylvania. Robert Holtz, Phillip Demas and Randy Creason worked as maintenance employees at the complex. After watching a TV program on the dangers of asbestos, the employees contacted management and asked whether they were being exposed to asbestos in their work. They were particularly concerned about one particular apartment in which they were working, where a water-damaged ceiling contained materials similar to what they had seen in the TV program. Management assured them there was no asbestos in the complex.

Still concerned, the employees obtained a sample of the materials they had been working with and had it tested at an independent lab. The test sample was positive for asbestos. With that result in hand, the employees asked management to do further testing, but management said no.

When the employees were instructed to return to the

particular apartment they refused, citing possible asbestos contamination. Odyssey Capital then fired the employees for insubordination and failure to perform their jobs as directed. That in turn prompted the employees to file unfair labor practice charges with the National Labor Relations Board.

The NLRB ruled that the firings were illegal. The employees' actions, said the NLRB, were "protected concerted activity" directed at bettering their working conditions. Only if concerted activity is "unlawful, violent, in breach of contract, or otherwise indefensible" may an employer take adverse action. Here, however, there was no claim by Odyssey Capital that the employees' refusal to work in the apartment fell in any of those categories. The fact that employers have the statutory right to fire "for cause" does not mean that an employer can adopt a work rule that effectively prohibits protected concerted activity.

It doesn't even matter, said the NLRB, whether an employee's concerted activity is objectively reasonable. In this case, for example, the employees' fears of asbestos exposure may or may not have been reasonable, but so long as they acted in concert with a view to bettering their working conditions, their actions were protected.

In reaching its conclusion, the NLRB relied on a 1962 Supreme Court decision involving a factory in Baltimore. In that case, seven employees had walked off the job on a bitter cold January day because their work area was unheated. The area was often uncomfortably cold anyway (a matter of repeated complaint) and, on the day in question, the furnace that usually supplied some heat had broken down. The Supreme Court held that the job action was protected under federal labor law and that the employer had no right to fire the workers.

Statutory reference. 29 U.S.C. § 151.

Case references. *Odyssey Capital Group, L.P.*, NLRB Case No. 6-CA-30010 (Aug. 1, 2002); *NLRB v. Washington Aluminum Co.*, 370 U.S. 9 (1962).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 19.08.

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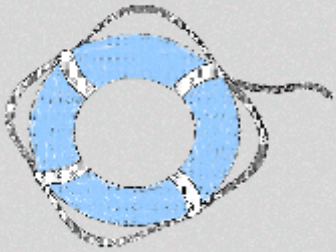

Employer Alerts!

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Written by the Attorneys at

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The "Motor Private Carrier" Overtime Exemption – Big Enough to Drive a Truck Through?

– by Charles H. Fleischer, Esq.

The Fair Labor Standards Act (FLSA), administered by the U.S. Department of Labor (DOL), requires employers to pay time-and-a-half for work by non-exempt employees that exceeds 40 hours in any workweek. The most common exemptions from the overtime requirement are for salaried executives, administrators and professionals, and for outside salespersons. But the FLSA has a whole list of other exemptions, ranging from agriculture to wreath making.

One exemption that has received little attention is for "motor private carriers." If a company's business includes making deliveries or carrying goods by motor vehicle, some of its employees may fall within this exemption, even though the company's primary business is completely unrelated to transportation.

Statutory Background

When Congress passed the FLSA in 1938, the Motor Carrier Act (MCA) was already on the books. The MCA provided for regulation of "motor carriers" and "private motor carriers" by the former Interstate Commerce Commission (now the Department of Transportation, or DOT). The term "motor carrier" is defined as a person providing motor vehicle transportation of goods or passengers *for compensation* in interstate commerce. It covers common carriers, such as bus companies, interstate van lines, and parcel delivery companies who serve the public generally, and contract carriers, such as trucking companies who haul under contract with specific shippers.

A "motor private carrier" is defined in the MCA as a person, other than a motor carrier, transporting property by motor vehicle in interstate commerce when the person is the owner, lessee or bailee of the property being transported and the property is being transported for sale, lease, rent or bailment, or to further a commercial enterprise.

The DOT has broad economic and licensing authority over motor carriers. With respect to motor private carriers, however, DOT's regulatory authority is limited to prescribing the qualifications and maximum hours of service of motor private carrier employees "when needed to promote safety of operation."

In enacting the FLSA, Congress could have sub-

jected employees of motor carriers and motor private carriers to hours-of-service regulatory authority of both the DOT and the DOL. But it decided not to do that. Instead, Congress included in the FLSA an exemption for "any employee with respect to whom the Secretary of Transportation has power to establish qualifications and maximum hours of service" – in other words, employees of motor carriers and motor private carriers. The exemption applies to employees over which DOT "has power" to regulate, even if DOT has not actually exercised that power by issuing regulations.

Who Is Engaged in Interstate Commerce?

For the exemption to apply, the employer must be engaged in interstate commerce. This makes sense, since the employer would not be subject to federal DOT or DOL regulation in the first place if he were not engaged in interstate commerce.

What does "interstate commerce" mean in this context?

Anyone who is transporting property across state lines for commercial purposes is engaged in interstate commerce. In the Washington, D.C. region, where three jurisdictions are in close proximity and where traveling from one jurisdiction to the other is often a daily occurrence, it should be easy to meet this test.

Even when the transportation takes place entirely within one state, a company is still engaged in interstate commerce if the goods being transported originated out of state, if the original shipper intended to ship them interstate, and if the local, in-state transportation is part of a "continuity of movement" of the goods from original shipper to ultimate customer.

Recent cases illustrate how these tests work. In each of these cases, the employees involved were exempt from FLSA overtime requirements.

! In *Klitzke v. Steiner Corp.*, the employee was a route salesman for a company that provided laundry and uniform rental and sales services in Eugene, Oregon. Even though the employee's route was entirely within the state of Oregon, over half his deliveries were of items purchased from out of state vendors. The Court held that the employer was engaged in interstate commerce.

! A beer distributor in Poughkeepsie, New York was also engaged in interstate commerce, where the distributor had obtained a federal ATF license to receive, sell and deliver malt beverages in interstate commerce and where its main supplier was Anheuser-Busch, headquartered in St. Louis, Missouri. It didn't matter that all the distributor's customers were located within New York State. *Bilyou v. Dutchess Beer Distributors, Inc.*

! In another New York case, a local distributor of Thomas' English Muffins was held to be engaged in interstate commerce because he obtained his muffins from a bakery in New Jersey. *McGuiggan v. CPC Int'l, Inc.*

! *Carpenter v. Pennington Seed, Inc.* involved a wholesale distributor of garden supplies, feed and grain. From its distribution facility in Ponchatoula, Louisiana, the wholesaler delivered products to customers in Texas, Louisiana, Mississippi, Alabama and Florida, using his own employees and trucks. This, too, was interstate commerce.

! CableData provided computer hardware and software, installation, maintenance and repair services to customers engaged in the cable television business. Its Pennsylvania regional office served customers throughout the mid-Atlantic states. CableData's field engineers, working out of Pennsylvania, regularly traveled to customer sites using their personal vehicles if the customers were no more than a four- to six-hour drive; otherwise, they flew and rented cars on their arrival. Since the engineers were transporting tools, component parts and equipment

when visiting customers, they, too, were engaged in interstate commerce. *Friedrich v. U.S. Computer Services.*

Which Employees Are Exempt?

DOT's power to regulate motor private carrier employees is tied to highway safety. So only those employees whose duties directly relate to safety of operation of motor vehicles are within DOT's jurisdictional power. However, the employee's duties need only *include* safety-related functions; the employees need not be engaged exclusively in such functions.

DOT has identified "drivers," "drivers' helpers," "loaders" and "mechanics" as affecting safety of operation. DOT has disclaimed power to establish qualifications or maximum hours of service for other employees of motor private carriers, such as stenographers, clerks, foremen, warehousemen, superintendents, salesmen, and employees acting in an executive capacity. To the extent DOT disclaims power to regulate, those employees *are not* within the exemption and they *are* subject to FLSA overtime requirements.

The term "drivers" includes persons who drive at least part of their time in interstate commerce, even though their primary duties may be unrelated to transportation. The field engineers who worked for CableData provide a good example. "Drivers" also includes individuals who ride along as assistants or relief drivers, even if they also perform other work, such as unloading.

A "driver's helper" may be an armed guard on an armored truck; a conductor on a bus; a person who acts as a flagman or spotter when a vehicle is crossing railroad tracks or entering, exiting or turning around on a highway; a person who assists in getting help or placing warning flares in case of breakdown; and a person who helps put on or remove tire chains.

"Loaders" are employees who have responsibility for properly loading motor vehicles so that they can be operated safely on highways. This includes planning and building a balanced load and placing, distributing and securing freight, where failure to do so could affect the safe operation of the vehicle. A checker, foreman or other supervisor who plans or immediately directs such activities may also be considered a loader. However, if the freight involved is light-weight, so that safety would probably not be affected no matter how the freight is loaded, the employees involved will not be considered "loaders." Similarly, employees who load bulk freight like coal by simply pouring it into a dump truck may not qualify as "loaders."

A "mechanic" is someone who keeps a motor vehicle in good and safe working condition. Employees who inspect, repair, adjust or maintain steering apparatus, lights, brakes, horns, wipers, wheels and axles, bushings, transmissions, differentials, starters, ignitions, carburetors, fifth wheels, springs, frames, and gasoline tanks qualify. So do employees who check tire pressure and change tires, who hook up tractors and trailers (including light

and brake connections) and who inspect such hookups. But persons who work as dispatchers or who do nothing but oil, gas or wash motor vehicles, fill radiators, or check batteries do not.

What About DOT Regulations?

DOT has power to prescribe the qualifications and maximum hours of service of all drivers, drivers' helpers, loaders and mechanics employed by motor private carriers. (It does not prescribe pay or overtime rates for motor private carrier employees.) It has not exercised that full authority, however. Currently, the DOT regulates hours of service of most drivers employed by motor private carriers (with certain exceptions); it exercises no regulatory authority at all over drivers' helpers, loaders or mechanics.

In general, drivers are prohibited from driving more than 10 hours following 8 consecutive hours off. In addition, drivers are prohibited from driving for any period after –

- having been on duty 15 hours following 8 consecutive hours off; or
- having been on duty 60 hours in any 7 consecutive days, if the carrier does not operate commercial motor vehicles every day of the week; or
- having been on duty 70 hours in any period of 8 consecutive days if the carrier does operate commercial motor vehicles every day of the week.

The absence of DOT regulations does not affect an employee's status as exempt for FLSA purposes, since it is the power to regulate, not the exercise of that power, that triggers the exemption.

State Wage and Hour Laws

The FLSA explicitly permits states to mandate greater overtime benefits than are required by federal law. Numerous cases have applied that provision to allow enforcement of state overtime requirements even though the employees work for motor carriers and are exempt from federal requirements.

Maryland and Virginia employers whose employees are covered by the motor carrier exemption need not worry about state overtime requirements: Maryland's wage an hour law exempts employees "for whom the United States Secretary of Transportation may set qualifications and maximum hours of service" and Virginia does not have any separate overtime pay requirement.

In the District, however, employees who are covered by the motor carrier exemption are still entitled to time-and-one-half for overtime: District law does require overtime pay, and it contains no exemption for motor carrier employees.

Conclusion

If your business involves the delivery by motor vehicle across state lines of goods you produce or acquire locally from others, or if it involves the local delivery by motor vehicle of goods acquired from out of state vendors, you may be engaged in interstate commerce. Even if it just involves transporting tools or equipment across state lines, you may still qualify. It doesn't matter that your primary business is unrelated to transportation. And if you are engaged in interstate commerce, your drivers and other employees who have direct responsibility for the safe operation of your vehicles may be exempt from time-and-a-half overtime requirements.

Determinations whether a particular company is engaged in interstate commerce and whether particular employees fall within the definition of "driver," "driver's helper," etc., are fact specific. While the examples and definitions given above provide guidance, a prudent employer will still want professional advice before concluding that FLSA overtime regulations don't apply.

Mistakes here can be costly. Failure to pay overtime can result not only in administrative action by federal or state regulators, but also in suits by the employees involved. If a large group of employees has been erroneously treated as exempt for a number of years, the price tag could amount to thousands of dollars. For Maryland employers the price tag can be even greater, since the courts there have authority to award treble damages for wage violations.

Even though an employee may be exempt from overtime pay requirements, the employee may still be covered by the minimum wage, child labor, and equal pay provisions of the FLSA.

Statutory references. 29 U.S.C. § 201 (FLSA); 49 U.S.C. § 13101 (MCA); Md. Code, L&E § 3-415; Va.Code § 40.1-28.8; D.C.Code § 32-1104.

Regulatory references. 29 C.F.R. § 782.0 (DOL regulations); 49 C.F.R. § 395.1 (DOT regulations).

Case law references. *Levinson v. Spector Motor Service*, 330 U.S. 649 (1947); *Bilyou v. Dutchess Beer Distributors, Inc.*, 300 F.3d 217 (2d Cir. 2002); *Klitzke v. Steiner Corp.*, 110 F.3d 1465 (9th Cir. 1997); *Friedrich v. U.S. Computer Services*, 974 F.2d 409 (3d Cir. 1992); *McGuiggan v. CPC Int'l, Inc.*, 84 F.Supp.2d 470 (S.D.N.Y. 2000); *Carpenter v. Pennington Seed, Inc.*, 2002 WL 465176 (E.D.La. 2002); *Overnite Transportation Co. v. Tianti*, 926 F.2d 220 (2d Cir. 1991); *Keeley v. Loomis Fargo & Co.*, 11 F.Supp.2d 517 (D.N.J. 1998); *Central Delivery Service v. Burch*, 355 F.Supp. 954 (D.Md. 1973), aff'd, 486 F.2d 1399 (4th Cir. 1973); *Williams v. W.M.A. Transit Co.*, 472 F.2d 1258 (D.C.Cir. 1972).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 4.02.

Trade Adjustment Assistance Recipients Entitled to Second Chance Under COBRA

– by Charles H. Fleischer, Esq.

When workers in a particular industry are adversely affected by an increase in imports of foreign goods, the Trade Act of 1974 has long allowed them, their unions, or their employer, to petition the Secretary of Labor for a determination that the workers are eligible for trade adjustment assistance (TAA) – basically, a continuation of unemployment insurance benefits once regular UI benefits have run out.

Under COBRA, when a "qualifying event" occurs, such as loss of a job or reduction in hours making the employee ineligible for employer-sponsored health insurance, the employee may elect COBRA continuation coverage. In general, the employer must notify the employee of COBRA availability within 14 days and the employee then has 60 days to elect COBRA coverage.

The Trade Act of 2002 now entitles TAA-eligible workers a second chance to elect COBRA. Workers who for whatever reason did not elect COBRA coverage following the original qualifying event now have an additional 60 days following their becoming TAA-eligible to elect COBRA coverage. This second chance election must be made within six months after the original, TAA-related loss of health insurance.

The new law does not specify what, if any, duty the employer has to notify workers of their second chance election. Presumably this will be clarified in Department of Labor regulations.

The new law does say that after a second chance election, coverage commences at the beginning of the new 60-day election period. In other words, coverage does not reach all the way back to the original qualifying event. It is not clear whether COBRA continuation coverage – which typically lasts up to 18 months follow-

ing a job loss – runs from the original qualifying event, or from the effective date of the second chance election.

HIPAA – the Health Insurance Portability and Accountability Act – is also affected. The new law says that if second chance COBRA coverage is elected, the period between the original, TAA-related loss of coverage and the commencement of second chance COBRA coverage does not constitute a break in coverage for preexisting condition computation purposes.

The new law applies to workers who become TAA-eligible on or after November 4, 2002.

Statutory reference. 19 U.S.C. § 2101 (Trade Act of 1974); Pub.Law 107-210, approved Aug. 6, 2002 (Trade Act of 2002); 29 U.S.C. § 1165 (COBRA).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 9.04

Employment Contract Dispute Successful But Costly

-- by Charles H. Fleischer, Esq.

When Atlantic Fabritech, located in Rockingham County, Virginia, hired Chuck Hiers as its sales manager, the parties typed up a one-page employment agreement that had the following provisions –

- Effective dates: August 14, 1998 – August 1, 2003;
- $25,000 annual salary plus cost-of-living increases;
- 2% commission on sales "quoted, processed, generated and sold by Chuck"; and
- "Thirty (30) days' notice will be given by both the employee and the employer in the case of leave or dismissal."

Not long after the employment began, disputes arose as to Hiers' commissions. Hiers claimed that he was entitled to commissions on all sales within his department; Atlantic said commissions were due only on Hiers' personal sales.

As a result of the commission dispute and other performance issues, Atlantic fired Hiers in May 1999. Hiers then sued Atlantic, saying he had a five-year employment contract that could only be terminated for just cause, and since Atlantic has no cause for termination, Hiers' termination was in breach of the contract.

Normally, when a contract dispute goes to court, the judge, not the jury, is responsible for interpreting the contract and deciding what it means. In interpreting the contract, the judge is normally limited to considering only the language contained within the "four corners" of the contract itself. However, when a contract is ambiguous (such as when it contains internally inconsistent provisions), the jury gets to decide what the contract means and the jury may consider evidence outside the four corners of the contract, including testimony as to what the parties intended the contract to mean. In the case of a contract dispute between an employer and an employee, it's usually to the employer's advantage to have the contract ruled clear and unambiguous; that way the employee doesn't gets to tell the jury what he thought the contract meant and play on the jury's sympathies.

In Hiers' dispute with Atlantic, the trial judge ruled that the contract was ambiguous. The trial court therefore permitted Hiers to testify about the commission arrangements he thought he had made and to claim that the contract was for a fixed, five-year term. The jury agreed with Hiers and awarded him $260,000 in damages.

On appeal, the Virginia Supreme Court reversed the trial court and said there was no ambiguity. Although the contract did provide for a five-year term, it also said that either party could terminate the contract on 30 days' notice. This second provision "trumped" the five-year provision, said the Court.

As to the commission issue, Hiers should not have been permitted to testify as to what he thought the arrangement was, since the contract clearly specified that commissions would be based just on his personal sales.

The employer here ultimately won, but it did so only after three years of litigation and after suffering all the costs, disruption and aggravation that go with litigation. The employer would have been much better off by devoting a little time and money beforehand to a contract that clearly preserved an employment at will relationship and that left no room for Hiers' claims. While no contract is completely bulletproof, this one would have benefitted from a bit more shielding.

Case reference. *Cave Hill Corp. v. Hiers*, 570 S.E.2d 790 (Va. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 1.04.

Maryland Employers Cannot Condition Incentive Pay on Continuing Employment

– by Lilliam L. Machado, Esq.

The Maryland Court of Appeals (Maryland's highest court) has issued an important decision regarding an employer's obligation to pay incentive compensation after an employee has quit or been terminated.

Many incentive compensation plans require employees to be employed on the date the commission or bonus is paid. The Court has now ruled that when incentive fees are part of an employee's promised compensation for work performed, but payment is not yet due at the time the employment ends, the fees must be paid in the normal course to the departed employee despite an express term in the employment contract or an employer policy to the contrary.

The Maryland Court of Special Appeals (Maryland's intermediate appellate court) ruled the same way last December. See "More on Wages and Treble Damages in Maryland," *Employer Alerts!* (Jan. 2002), p. 5.

The case involved Timothy McCabe who worked for Medex under an employment contract that provided:

> Payment from all Company incentive compensation plans is conditioned upon meeting targets and the participant being an employee at the end of the incentive plan (generally the fiscal year) and being employed at the time of actual payment.

The fiscal year involved in the case ended on January 31, 2000, but payments under the incentive plan did not occur until March 31, 2000. McCabe, who had resigned in early February, made a claim for his incentive fees through January 31. Medex, relying on its stated policy, refused to pay. Medex argued that its incentive fees were not simply commissions, but more akin to a bonus for continued employment.

The Court rejected Medex's argument. Looking to Maryland's wage and hour law (which defines "wage" to include bonuses, commissions, fringe benefits, and "any other remuneration promised for service"), the Court ruled that McCabe's incentive fees were directly tied to his sales and they therefore were wages.

Another provision of Maryland law requires an employer to pay wages to a terminated employee on or before the date the employee would have been paid but for the termination. Since McCabe had performed all work necessary to earn the fees and Medex had even registered the sales on which the fees were based, the fees had to be paid. The additional requirement that McCabe be employed on the date of payment was contrary to Maryland's wage and hour law and was therefore unenforceable.

The Court dealt with yet another provision of Maryland law that allows an employee or former employee to sue his employer not only for unpaid wages, but also for treble damages and for the employee's attorneys' fees. Medex argued that its failure to pay McCabe was based on a "bona fide dispute" over what was due and therefore, under the law, it should not have to pay treble damages. The Court said the question whether a bona fide dispute exists should have been submitted to a jury and it sent the case back to the trial court in Baltimore for that purpose.

All employers subject to Maryland law who pay incentive compensation will want to take a close look at their plans in light of this new case. While it may still be possible, under limited circumstances, to condition certain payments to continued employment, existing plans are probably inadequate and will likely fall victim to the Court's new ruling.

Statutory reference. Md. Code, L&E § 3-501.

Case reference. *Medex v. McCabe*, 2002 WL ____ (Md. No. 2, decided Nov. 14, 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 4.03.

Employer's Phone Monitoring May Violate Federal Wiretap Act

-- by Charles H. Fleischer, Esq.

We have all heard the recorded announcement, "This call may be monitored for quality assurance purposes." If we don't want our call "monitored" (that is, listened to by some anonymous third person, or recorded for later review), we hang up. Presumably, if we proceed with the call, we consent to the monitoring.

When an employee is hired by a company that practices call monitoring, the employee is typically informed of the policy. By taking the job, the employee is considered as consenting to the practice as well.

Do these procedures protect the employer from claims under the federal Electronic Communications Privacy Act? Not necessarily, as shown by a recent decision from the U.S. District Court for the District of Maryland.

Salima Rassoull worked for Maximux, Inc., assisting social security beneficiaries in their efforts to re-enter the workforce. Her duties included answering incoming calls from beneficiaries and making with outgoing calls when necessary. She knew that her phone conversations were monitored "for quality assurance purposes" and understood the policy, but she believed the monitoring applied only to business calls, not personal calls.

On April 17 and 18, 2001, Rassoull was ill and stayed home from work. Her friend and co-worker at Maximus, Karen Reddon, called Rassoull at home, using Maximus' office phone. Reddon worked in a different department from Rassoull and she apparently was not familiar with or subject to Maximus's monitoring policy.

According to Rassoull's lawsuit, during the phone conversations Reddon and Rassoull criticized a Maximus dress policy, they discussed a disagreement that Rassoull had had with her supervisor, and they talked about a funeral Rassoull was planning to attend later in the week. Although the conversations related in part to work, they clearly were not in furtherance of either Reddon's or Rassoull's jobs and were considered by the Court as personal. On both occasions, supervisory personnel listened to the entire conversation and even invited others to listen on a speakerphone for approximately three minutes.

When Rassoull returned to work she learned about the alleged monitoring and became very upset. According to Rassoull, the incident aggravated her pre-existing

bipolar disorder and caused her acute stress. Efforts to be transferred failed and she ultimately quit. She then brought suit under the Electronic Communications Privacy Act.

The ECPA makes it illegal for any person intentionally to intercept any wire, oral or electronic communication. It is also illegal to intentionally disclose any communication obtained in violation of the ECPA.

Maximus argued that its actions fell within an exception to the ECPA, which permits interception where at least one party to the conversation consents. According to Maximus, Rassoull knew about and implicitly consented to monitoring of phone calls, making the interception in this case perfectly legal. (Although the ECPA is a so-called "one-party consent statute," some states, including Maryland, have wiretap statutes which require the consent of all parties to the conversation. See "Employer 'Tripps' on Maryland Wiretap Act," *Employer Alerts!* (June 2002), p. 5.)

The Court disagreed with Maximus. Under the Court's analysis, the only monitoring Rassoull may have consented to related to business calls made or received while at work. She had no reason to know about, or consent to, monitoring of personal calls while she was at home.

Another exception to the ECPA, involving use of monitoring equipment in the ordinary course of Maximus's business, was also inapplicable. Assuming that the monitoring of business calls "for quality assurance purposes" can fall within the so-called "business use" exception, the phone calls here at issue clearly were personal. While an employer cannot perhaps know in advance whether a particular call is business or personal, an employer can certainly make that determination after briefly intercepting the call. Three minutes of monitoring, said the Court, was too long.

Statutory reference. 18 U.S.C. § 2510.

Case reference. *Rassoull v. Maximus, Inc.*, 209 FRAT 372 (D.Md. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 13.05.

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In this issue of *Employer Alerts! ...*

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Employer Alerts!

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Workers' Comp and the Second Injury Fund

Suppose an employee has a serious, pre-existing condition, but is nevertheless able to work. Some employers may be reluctant to hire him, fearing that a subsequent injury on top of the earlier condition, even if minor, could disable him and expose the employer to liability for permanent workers' comp disability benefits.

To overcome an employer's reluctance in this situation, many jurisdictions have created a special fund that reimburses the employer for a portion of the comp benefits due a re-injured employee. Each of the three local jurisdictions has such a second injury fund, although computation of the reimbursement amount differs from jurisdiction to jurisdiction.

In *Maryland*, when an employee with a pre-existing permanent impairment suffers a subsequent injury or illness resulting in permanent disability greater than 50%, the employee is entitled to comp benefits based on the combined effect of the pre-existing condition and the subsequent injury or illness. However, the employer is only liable for benefits that would have been due from the second injury or illness alone. The special fund (which Maryland calls its "Subsequent Injury Fund") picks up when the employer's obligation ends.

When a *Virginia* employer pays compensation for a disability resulting from the combined effect of two impairments, the employer may claim reimbursement from the Second Injury Fund for a pro rata share of benefits. Employers must notify the Fund of their reimbursement claim prior to actually paying benefits.

In the *District*, the employer is liable to pay compensation as if the second injury alone caused the disability, but the employer's obligation ends after 104 weeks. The special fund assumes liability for payment of benefits for subsequent weeks.

A recent District of Columbia case dealt with the issue whether the employer has to know about the pre-existing condition at hiring time to take advantage of the second injury fund. Arguably, an employer who does not know about an applicant's pre-existing condition does not need the incentive of a second injury fund to overcome his natural reluctance to hire the applicant. In other words, goes the argument, only employers who know about the pre-existing condition at hiring time should be able to claim benefits from the fund later on when the subsequent injury occurs.

The case before the D.C. Court of Appeals

involved Adolph Notel, a local laborer who had suffered several ankle injuries while working construction for a prior employer. In 1990, while working at a new company, he injured his ankle again and was awarded permanent partial disability under the District's workers' comp statute. Medically, 60% of the award was attributed to the most recent injury and the remaining 40% was attributed to prior injuries and to degenerative arthritis.

Notel's current employer paid almost $35,000 in permanent partial disability benefits and another $1,890 for medical expenses. The employer then made claim under the District's second injury fund for partial reimbursement. The Department of Employment Services (DOES) denied reimbursement because there was no evidence that the employer had actual knowledge of Notel's prior injuries before hiring him. The employer appealed DOES's denial to the D.C. Court of Appeals.

The Court first reviewed the purpose of the fund – to "prevent and reduce employment discrimination based on the risk of disability-related liability." According to the Court, workers' comp statutes inadvertently create a perverse disincentive which second injury funds are designed to eliminate.

The Court then upheld the DOES decision and agreed that the employer should not get reimbursement from the second injury fund, but the Court rejected DOES's "actual knowledge" requirement. The Court said the proper test is whether a pre-existing condition is "manifest" – that is, whether the condition "puts the employer on notice of greatly increased liability and thus creates a risk of discrimination." Of course, a condition is manifest when an employer does in fact have actual notice of the condition. But a condition will also be considered manifest "when a reasonable person in the employer's shoes would have known about that condition."

Other cases applying the "manifest" requirement have said, for example, that the requirement is satisfied when the pre-existing condition is disclosed in medical records that are available to the employer prior to the subsequent injury. Here, however, there was no evidence that the employer either knew about Notel's prior ankle injuries or that medical records disclosing the injuries were available to the employer. Therefore, Notel's pre-existing condition was not "manifest" and the employer could not recover from the second injury fund.

Had Notel's employer required a medical exam at hiring time, it probably would have learned about the prior injuries and later been able to show that Notel's condition was manifest. Medical exams must, of course, be conducted in compliance with ADA requirements.

Statutory references. Md. Code, L&E § 9-801; Va. Code § 65.2-1100; D.C. Code § 32-1508.

Case reference. *Mergentime Perini v. D.C. Dept. of Employment Services*, 2002 WL 31662789 (D.C. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 7.04.

Alternative Overtime Arrangements

The Fair Labor Standards Act (FLSA) generally requires employers to pay non-exempt employees compensation for time worked in excess of 40 hours per workweek at the rate of one and one-half times the employee's regular hourly rate for that workweek. An employee who earns $10 per hour and works 50 hours in a particular workweek is entitled to $550 ($400 + $15 x 10). Private sector employers generally cannot use "comp time" (time off) to satisfy their overtime obligations.

Employers do not have to pay overtime to "exempt" employees. See, for example, "The 'Motor Private

Carrier' Overtime Exemption – Big Enough to Drive a Truck Through?," *Employer Alerts!,* Dec. 2002, p. 1. But even for non-exempt employees, there are a number of methods for dealing with overtime that may simplify the employer's bookkeeping or even reduce the employer's costs.

Comp Time in Same Workweek

A "workweek" is any seven consecutive 24-hour periods (168 hours) as determined by the employer. A typical workweek begins on Sunday at 12:01 a.m. and ends the following Saturday at midnight. If an employee works more than 40 hours in that workweek, the employer's overtime obligation is triggered. It does not matter whether the employer pays on a weekly, bi-weekly, or some other basis.

While an employer generally cannot offer comp time in workweek #2 for overtime hours worked in workweek #1, the employer can offer comp time in the same workweek. So if an employee works 10 hours on Monday, the employer could have the employee work only 6 hours on Tuesday. Assuming the rest of the week the employee works his customary 8-hour day, total hours worked in the workweek are 40 and no overtime obligation is incurred.

Time Off Plan

There is one exception to the rule that comp time in workweek #2 does not satisfy the employer's obligation for overtime in workweek #2 – a so-called "time off plan." Suppose an employer pays on a bi-weekly basis. If a non-exempt salaried employee works overtime in workweek #1, the employer can give the employee time off in workweek #2 at the rate of one and one-half hours for each hour of overtime worked in workweek #1. By paying the employee his regular salary for both workweeks, the employer fully satisfies his overtime obligation.

For example, suppose the employee normally works 40 hours per workweek and is paid a bi-weekly salary of $800 ($400 per week). If the employee works 50 hours in workweek #1, the employee can take (or be ordered to take) 15 hours off in workweek #2, since 1.5 times the 10 hours of overtime worked in workweek #1 equals 15. In this example, the employee has worked a total of 65 hours over both workweeks and will be paid his regular bi-weekly salary of $800. In effect, the employer satisfies his overtime obligation by paying *comp time* at a premium rate instead of paying a *cash* premium.

A time off plan only works if the employer's pay period is longer than one workweek and if overtime occurs in the first workweek. In the above example, if the overtime occurred in workweek #2, the employer would have to pay the overtime premium in cash.

Belo Plan

"Belo" plans (from a Supreme Court case of that name), are available only for employees whose duties necessitate irregular hours because of the nature of the work. Examples might include on-call service workers and emergency repair crews. Under a Belo plan, the employer enters into a contract with the employee which guarantees the employee a fixed salary regardless of the number of hours worked. The contract specifies a regular hourly rate for the normal 40 hours and one and one-half times that regular hourly rate for guaranteed overtime (so long as total time covered by the plan is no more than 60 hours per workweek).

For example, suppose a power company employee's job is to restore electrical service following outages caused by storms, traffic accidents, construction mishaps, etc. The amount of work needed is unpredictable, typically varying anywhere from 30 hours per workweek up to 50. So the employer enters into a contract guaranteeing the employee a fixed weekly salary of $550, representing 40 hours at $10 per hour and 10 hours at a $15 overtime rate. In other words, the contract guarantees the employee 10 hours of overtime each week. Then, regardless of the number of hours worked (up to the agreed total of 50 hours in this example), the employer has no additional overtime obligation. Of course, if the employee works less than 50 hours, he still gets paid his $550.

In the above example, any time worked in excess of 50 hours would have to be compensated at $15 per hour. While the parties could have agreed to guaranty more than 10 hours of overtime, their agreement could not go beyond 20 hours of overtime under a Belo plan.

Half-Time (Fluctuating Workweek) Plan

Belo plans, discussed above, are only available where the inherent nature of the work necessitates irregular hours and where the number of hours per workweek vary both above and below a normal 40-hour workweek. In contrast, under a half-time plan (sometimes called a fluctuating workweek plan), the fluctuation can be under the employer's control and hours worked can routinely exceed 40.

Under a fluctuating workweek plan, the employer and employee agree that the employee will be paid a fixed salary covering all time worked in the workweek. This should be a written agreement by which the employee clearly acknowledges that the fixed salary covers the straight-time component of all hours worked, even if they exceed 40. For any given workweek, the employee's regular hourly rate is computed by dividing the fixed salary by the number of hours actually worked in that workweek. If the number of hours worked exceeds 40, the employer pays the employee one-half (not one and one-half) of his regular hourly rate for the hours exceeding 40. The reason the employer pays only half-time for the overtime is that the straight-time component is already covered by the fixed salary.

To illustrate, suppose the employer and employee agree to a fixed salary of $400 per week. If in a particular workweek the employee works 50 hours, then the employee's regular hourly rate for that workweek is $8 ($400 ÷ 50). Therefore, the employer's overtime obligation for that workweek is $40 (½ of $8 x 10) and total compensation due the employee for that workweek is $440.

Now suppose the employee works 55 hours. His regular hourly rate would then be approximately $7.27 ($400 ÷ 55) and the total compensation due would be $454.53 ($400 + ½ of $7.27 x 15 hours). As this example shows, as overtime increases the regular hourly rate, and therefore the overtime rate, decrease.

If the employee worked 80 hours in a particular workweek, his regular hourly rate would then drop to $5.00 per hour, which is below the minimum wage of $5.15 and which would therefore violate federal law. The fixed salary

under a half-time plan must be high enough to guaranty at least the minimum wage.

Statutory reference. 29 U.S.C. § 201.

Regulatory reference. 29 C.F.R. Part 548.

Case references. *Walling v. A. H. Belo Corp.*, 316 U.S. 624 (1942); *Bay Ridge Operating Co. v. Aaron*, 334 U.S. 446 (1948); *Dunlop v. New Jersey*, 522 F.2d 504 (3d Cir. 1975), *rev'd on other grounds sub nom. New Jersey v. Usury*, 427 U.S. 909 (1976); *Highlander v. K.F.C. Nat. Mgmt. Co.*, 805 F.2d 644 (6th Cir. 1986).

EMPLOYER'S SURVIVAL GUIDE **reference.** 4.02.

DOL Proposes Repeal of Birth and Adoption Unemployment Insurance

The Clinton administration's Department of Labor initiated an experimental program allowing states on a purely voluntary basis to expand unemployment insurance (UI) coverage to workers who took time off to be with their newborn or newly adopted children. See "Birth and Adoption Unemployment Insurance," *Employer Alerts!*, July 2000, p. 1. Under the program, issued as Rule BAA-UC, participating states could allow unemployed workers to collect UI benefits even though the workers were unemployed voluntarily and were not available for work.

No state actually adopted legislation to take advantage of the BAA-UC program. H.B. 593, introduced in the Maryland General Assembly during the 2002 legislative session to participate in the experiment, never passed.

The Department of Labor now wants to repeal the program, citing the need to protect shrinking unemployment reserves. According to DOL, 28 states had less than 12 months of benefits in reserve at the end of 2001, 13 states raised taxes this past January to cover UI costs, and at least six states will likely have to borrow to replenish UI trust fund balances.

The proposed repeal is open for comment until February 3, 2003.

Statutory reference. 26 U.S.C. § 3301.

Regulatory references. 20 C.F.R. § 604; OPA News Release 12/03/02.

EMPLOYER'S SURVIVAL GUIDE **reference.** 8.03.

Cash Balance Conversion Moratorium to Be Lifted

In another Bush administration initiative, the Clinton-era moratorium on approvals of cash balance plan conversions would be lifted under regulations proposed by the Treasury Department.

In recent years a number of companies, including most notably IBM, have converted their more traditional defined benefit pension plans to cash balance plans. While there is nothing inherently wrong with a cash balance plan, *converting* to a cash balance plan is sometimes seen as age discrimination.

Under a defined benefit plan, the eventual retirement benefit is usually tied to some formula that includes factors for highest salary and years of service. Since those formulas produce a significant increase in benefits during the last several years of an employee's career, defined benefit plans are said to be "back-loaded." Cash balance plans, on the other hand, typically accrue benefits at a more level rate, so that in a conversion from a defined benefit plan to a cash balance plan, older employees miss out on the jump in benefits

they were expecting. See "Cash Balance Plans – What's All the Fuss About?," *Employer Alerts!*, Sept. 2001, p. 2.

Claims of age discrimination have also been aimed at the "wear-away" aspect of some conversions. If the monthly benefit produced by a defined benefit plan formula before conversion is greater than the anticipated monthly benefit produced by the cash balance plan formula after conversion, then future employer contributions are sometimes frozen until the cash balance plan formula catches up. Again, older workers were seen as disadvantaged by wear-away.

In the face of hundreds of age discrimination claims, the IRS under President Clinton imposed a moratorium on issuing determination letters approving conversions. The IRS under President Bush has now issued proposed regulations that, among other things, would validate conversions under most circumstances. With respect to wear-away, however, the regs would require that the opening account balance under the cash balance plan be at least equal to the "actuarial present value of the participant's prior accrued benefit, using reasonable actuarial assumptions." In other words, starting values for the new cash balance plans would have to be the actuarial equivalent of the old defined benefit plan. This requirement should solve most wear-away objections.

Conversions that comply with the proposed regs would be free from claims of age discrimination.

Hearings on the proposed regs are set for April 10, 2003 at IRS headquarters in Washington.

Statutory reference. 26 U.S.C. §§ 401, 411.

Regulatory references. Reg. 209500-86; Reg. 164464-02.

***EMPLOYER'S SURVIVAL GUIDE* reference.** 9.02.

Some Maryland County Discrimination Laws Ruled Unenforceable

Title VII of the federal Civil Rights Act prohibits discrimination in employment, but it applies only to employers who have 15 or more employees. The administrative remedies available under Maryland's employment discrimination laws are also available only to employers with 15 or more employees. (An employee who is *fired* or *forced to quit* for discriminatory reasons in Maryland can sue for abusive discharge even if the employer has fewer than 15 employees.)

The 15-employee threshold in federal and Maryland law has prompted a number of counties to adopt their own employment discrimination ordinances. The Montgomery County Code, for example, prohibits discrimination by *any* employer, even if he has only *one* employee. County ordinances sometimes expand the list of factors that are considered discriminatory, and they may permit recovery of damages beyond the amounts available under federal or state law. Typically, these ordinances provide both an administrative procedure and the right to sue for discrimination in state circuit court.

Do Maryland counties have authority to adopt such ordinances?

Maryland's Constitution, along with implementing legislation, grants Baltimore City and charter counties the right of self-government. Their powers, however, are limited to enacting "local laws." Any law which purports to apply outside the territorial limit of a particular county is not "local" and is therefore invalid. So, too, are laws that deal with the general public welfare or that affect the state as a whole.

In a pair of 1990 decisions, the Maryland Court of Appeals (the state's highest court) held that abusive employment practices constitute a statewide problem

already addressed by the General Assembly. Further, the creation of a new judicial cause of action encroaches upon state authority. Therefore, while counties may provide *administrative remedies* for employment discrimination within their borders, they may not authorize private individuals to sue in *state court*.

In response to those decisions, the Maryland legislature passed statutes authorizing civil suits for violations of anti-discrimination ordinances in Montgomery, Prince George's, Howard and Baltimore Counties, but not elsewhere.

In a recent case, an employee of H. P. White Laboratory brought suit for employment discrimination relying in part on Harford County's anti-discrimination ordinance. The Court of Appeals pointed out that the ordinance was almost identical to Montgomery County's, which the Court had previously held unenforceable in state court. The Court also pointed out that Harford was not on the list of counties whose anti-discrimination laws the General Assembly had blessed. Therefore, said the Court, Harford County's ordinance was invalid to the extent it purported to authorize employment discrimination lawsuits in court.

The General Assembly may, of course, see fit to expand the list of charter counties whose anti-discrimination ordinances are enforceable in court. However, unless and until it does, state courts have no authority to enforce such ordinances except in Montgomery, Prince George's, Howard and Baltimore Counties.

Statutory references. Md. Const., Art. XI-A § 2; Md. Code, Art. 25A § 5.

Case references. *McCrory Corp. v. Fowler*, 570 A.2d 834 (Md. 1990); *Sweeney v. Hartz Mountain Corp.*, 573 A.2d 32 (Md. 1990); *H. P. White Laboratory, Inc. v. Blackburn*, 2002 WL 31761391 (Md. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 11.05

Social Security Administration Simplifies Electronic W-2 Filing for Small Employers

For businesses with fewer than 20 employees, electronic filing of W-2 forms has now been streamlined. The process involves registering online at SSA's website to get a PIN. A password will then be mailed within 10 to 14 days. With the PIN and password in hand, the employer then returns to SSA's website, logs on, and creates and files electronic W-2s. Copies can be printed for distribution to employees.

To register, go to www.ssa.gov/ and select Business Services Online (formerly Employer Services Online). The entire process along with other information is explained in SSA's Handbook, also available at the website.

***EMPLOYER'S SURVIVAL GUIDE* reference.** 5.04

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Employer Alerts!

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Training as Additional Element of Sexual Harassment Defense

Almost five years ago the Supreme Court explained how employers could avoid liability for some types of sexual harassment in the workplace. The Court said that if an employer exercises reasonable care to prevent, and promptly correct, any sexually harassing behavior, and a victim of harassment unreasonably fails to take advantage of opportunities provided by the employer, then the employer would not be liable for the harassment.

What must an employer do to show he exercised "reasonable care"? In early 2001 the U.S. Court of Appeals for the Fourth Circuit (which governs Maryland and Virginia) decided a case in which the employer established and publicized a sexual harassment policy. Although the victim in that case knew about the policy, she failed to complain when her supervisor sexually harassed her over a period of several months.

The Fourth Circuit rejected the victim's claim of harassment, saying that the employer's distribution of an anti-harassment policy provides "compelling proof" that the company exercised reasonable care in preventing sexual harassment. See "Defending Sexual Harassment Claims," *Employer Alerts!*, April 2001, p. 5.

As comforting as the Fourth Circuit decision may be, it is probably not the last word. A recent New Jersey Supreme Court case ruled that despite a company policy against sexual harassment, an employee's claim for harassment had to go to trial over the factual question of just how effective the policy was.

The employer in the New Jersey case was the County of Hudson, which operates the Hudson County Jail. Maria Gaines, a guard at the jail, brought suit against the County under New Jersey's discrimination law, claiming that her supervisor, Captain Joseph Bellino, harassed her by forcible kissing her on one occasion. He also brought up the kissing incident a number of times in front of other employees and he even threatened to rape her. Although Gaines had told co-workers about the original kissing incident, she never filed a formal complaint with the County.

The County responded to the lawsuit saying that it had an anti-harassment policy in place, which Gaines failed to take advantage of. Therefore, according to the County, it should not be liable.

The lower courts agreed with the County and

dismissed Gaines' suit, but on appeal the New Jersey Supreme Court said there were factual issues that had to be tried. The Court pointed to evidence that despite the existence of an anti-harassment policy, the County failed to train any of its employees concerning the policy. The absence of training, said the Court, could support the conclusion that the County did not have an *effective* and *realistic* anti-harassment policy and that the policy was one in name only.

Although the decision is binding only in New Jersey, it may point the way for other courts to follow. A prudent employer will therefore want to take all the following steps to reduce the risk of liability for workplace sexual harassment –

- Establish a written non-discrimination policy, including a specific policy against sexual (and all other forms of) harassment. The policy should define sexual harassment and it should be published in the employee handbook and posted conspicuously at the workplace.

- Include in the policy various means by which an employee can complain in confidence about sexual harassment. The complaint route should not be limited to the employee's immediate supervisor, since he or she may be the harasser.

- Consider installing an anonymous hotline for employees to report harassment and other types of workplace problems.

- Conduct regular training seminars on sexual harassment, attendance at which should be mandatory. (It usually makes sense to have separate sessions for supervisors and non-supervisory personnel.)

- Keep careful records of who attended each training session and what material was presented.

- Plan in advance *who* will be in charge of investigating complaints of sexual harassment and *how* the investigation will be conducted. (Making those determinations after a complaint is received will cause delay and could result in your harassment policy being ruled unreasonable or ineffective.)

- On receipt of a complaint of sexual harassment, check your Employment Practices Liability Insurance policy and decide whether notice to your insurance carrier is required at this point.

- If the complaint involves sexual assaults or other criminal conduct, suggest that the complaining party make a police report.

- For serious, ongoing incidents, consider temporarily reassigning the alleged harasser or complaining party, or placing one or both of them on temporary leave with pay, to prevent additional incidents pending your investigation. (This could be a perilous step, since reassignment or leave might be construed as retaliation against the complainant or even defamation of the alleged harasser.)

- Investigate all complaints of sexual harassment promptly, thoroughly and objectively.

- Include an interview of the complaining party in the investigation. Get as much detail from him or her as possible about what happened, when and where it happened, and who else saw or knows about the harassment. Also, ask the complainant how he or she would like the matter to be resolved (without making any promises at this point about what action will be taken).

- Treat as confidential all information developed during the investigation. However, do not *promise* confidentiality, since complete confidentiality is probably not possible.

- Make a contemporaneous, detailed written record of the investigation.

- If the investigation shows that the complaint is justified, take prompt corrective action against the harasser. Inform the complaining party about the action taken and ask whether there is anything further he or she wishes to bring to the employer's attention.

- If the investigation shows the complaint to be unfounded, inform the complaining party and the accused harasser and close the investigation.

- Do not take disciplinary action against the complainant unless it is clear that he or she intentionally lied about the matter. (Retaliation against an employee for exercising rights protected by law, such as the right to complain about harassment, itself constitutes illegal discrimination.)

The risks faced by employers in this arena are substantial. So it makes sense to consult with competent employment law counsel for help with developing a reasonable and effective sexual harassment policy, designing a training program, and conducting any investigations that become necessary.

Case references. *Barrett v. Applied Radiant Energy Corp.*, 240 F.3d 262 (4th Cir. 2001); *Gaines v. Bellino*, 801 A.2d 322 (N.J. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.03.

Trans-Gender Claims Under FMLA, ERISA and Title VII

In two recent cases – both decided at the federal court of appeals level – employees who underwent sex change operations had their claims for a variety of work-related benefits denied.

Terry Sanders, who worked for May Department Stores in Missouri, suffered from "gender dysphoria." Born a male, Sanders desired to live and be accepted as a member of the opposite sex. Consistent with that desire, Sanders scheduled gender reassignment surgery.

Sanders told her employer she intended to quit her job well in advance of the surgery and that after the surgery she would be moving out of state to live with her new partner. The employer responded that Sanders "might" qualify for leave under the Family and Medical Leave Act, provided she furnish medical certification of the need for leave. Sanders said that due to confidentiality concerns, she did not want to provide a FMLA medical certification. Instead, she would just take the 13 weeks of personal leave that she had accrued and then quit.

After Sanders had the surgery, her personal plans apparently changed because she requested reinstatement at May Department Stores. May had not reserved Sanders' prior position, so it rehired her for a different position.

Several months later, May fired Sanders for poor performance in the new position. That's when Sanders sued May for allegedly violating FMLA by failing to offer her the 12 week's leave she might have been entitled to under the statute.

The case went to a jury trial in federal court, where Sanders' claims were rejected. On appeal, the U.S. Court of Appeals for the Eighth Circuit (headquartered in St. Louis) affirmed, saying that Sanders was adequately notified of the possibility that FMLA leave was available, but she voluntarily rejected it, opting instead to resign after taking personal leave

In deciding the case as it did, the Eighth Circuit did not reach the question whether gender dysphoria and sex change surgery constitute a "serious health condition" sufficient to trigger FMLA coverage.

* * *

Marc Mario (formerly Margo Mario), who also

suffered from gender dysphoria, underwent drug therapy and surgery to transform from female to male. He informed his employer, P & C Food Markets of western New York State, of his plans and, with the employer's permission, began to dress and present himself as a male.

Following the surgery, Mario submitted his medical bills for payment under P&C's self-insured group health plan. P&C denied the claim on the basis that the surgery was not medically necessary. So Mario sued for benefits under the Employee Retirement Income Security Act. (Like most group plans, P&C's plan was governed by ERISA.) He also sued under Title VII of the Civil Rights Act, claiming that denial of benefits amounted to a form of sex discrimination.

The court of appeals' opinion discusses at some length who, as between Mario and P&C, had the burden of proof as to medical necessity: did Mario have to prove that the treatment *was* medically necessary? or did P&C have to prove it *was not*?

Ultimately, because of the particular wording of the insurance policy involved, the court concluded that P&C had the burden of showing trans-gender surgery is *generally not* medically necessary. Here, P&C met the burden by offering testimony of a psychiatrist that the surgical removal of healthy organs, for no purpose other than gender dysphoria, fell into the category of cosmetic surgery and therefore *was not* medically necessary.

Once P&C met its burden, then Mario had the opportunity to show that his particular case was different from the ordinary situation and was in fact medically necessary. Since Mario offered no such evidence, he could not collect the insurance benefits he was after.

Mario's sex discrimination claim failed as well. Mario based his claim on a theory that he failed to conform to gender stereotypes (though born a female, he dressed and acted like a male), and it was for that reason P&C denied him insurance benefits. The court questioned whether trans-sexuals are even members of a protected class under federal anti-discrimination laws. But without deciding that question, it ruled that P&C's motive for denying benefits was not based on Mario's transsexualism but on the simple fact that the expenses were not medically necessary.

Could Mario have sued under the Americans with Disabilities Act, claiming that he was disabled under the ADA and that P&C's failure to provide insurance coverage constituted illegal discrimination? The answer is no, because the ADA defines "disability" to exclude "transvestism, transsexualism, pedophilia, exhibitionism, voyeurism, gender identity disorders not resulting from physical impairments, or other sexual behavior disorders."

Case references. *Sanders v. May Dept. Stores Co.*, 2003 WL 61112 (8th Cir. 2003); *Mario v. P&C Food Markets, Inc.*, 2002 WL 31845877 (2nd Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 12.03.

Virginia Restrictive Covenant Fails Again

Virginia courts have a discouraging track record when it comes to enforcing non-compete and other types of restrictive covenants against former employees. In August 2001, we reported on a Virginia Supreme Court decision that a covenant preventing a former employee from working in the same industry in which the employer was engaged was too broad. See "Virginia Supreme Court Rejects Non-Compete Covenant as Overbroad," *Employer Alerts!*, Aug. 2001, p. 2.

Less than a year later, that same court held there is no such thing as a restrictive covenant that is reasonable on its face. Instead, no matter how reasonable the covenant may appear, the employer still bears the burden of showing, on a case-by-case basis, why his

business needs the protection of a restrictive covenant. See "Non-Compete Covenants Faring Poorly in Virginia," *Employer Alerts!*, June 2002, p. 8.

The U.S. District Court that sits in Virginia, applying state law to an employer-employee controversy, also ruled last year that a restrictive covenant signed by an *existing employee* (as opposed to a new hire) was unenforceable because the employee didn't get any consideration in exchange. The mere continuation of at-will employment was not enough; the employer had to offer some "fresh consideration" like a promotion, salary increase, or even an employment contract.

A more recent decision continues this unfortunate trend.

MicroStrategy, of northern Virginia, brought suit to enforce a non-solicitation clause in employment agreements that it had with former employees. The clause read –

> I agree that for a period of one (1) year after termination of my employment with MicroStrategy for any reason, I will not, directly or indirectly, seek to influence any employees, agents, contractors or customers of MicroStrategy to terminate or modify their relationship with MicroStrategy.

MicroStrategy claimed that certain employees were recruited to work for a competitor named Business Objects in order for Business Objects to gain access to confidential MicroStrategy information and that the recruitment violated its non-solicitation clause.

The case was heard by the U.S. District Court. The Court first pointed out that, under Virginia law, restrictive covenants such as non-compete clauses and non-solicitation clauses are enforceable if they are reasonable. Reasonableness, in turn, depends on the following three factors –

- Whether the restraint is no greater than necessary to protect some legitimate business interest of the employer;
- Whether the restraint is unduly harsh and oppressive in curtailing the employee's legitimate efforts to earn a livelihood; and
- Whether the restraint is reasonable from the standpoint of sound public policy.

In this case, said the Court, the restraint was reasonable in terms of duration, since Virginia cases have upheld clauses that lasted much longer than one year.

However, said the Court, the clause is ambiguous in its scope. According to the Court, former MicroStrategy employees have no real yardstick to measure what actions might influence a customer to modify its relationship with MicroStrategy and cause the former employee to be in violation of the clause. Does the clause prohibit a former employee from engaging in legitimate competition by, for example, developing a better product that "influences" MicroStrategy custom-

ers to switch vendors? Former employees might feel prohibited from seeking any job in the same industry for fear that their work might somehow affect the relationship between MicroStrategy and its customers. Therefore, ruled the Court, the clause is at least potentially overbroad and unenforceable.

The only encouraging part of the decision is that the Court agreed to apply a "savings clause" contained in the employment contract. The savings clause here said that if any provision of the contract is ruled invalid, that invalidity will not affect the remaining provisions of the contract. The Court observed that existing Virginia cases on the effect of a savings clause are in conflict, but that the better rule in these circumstances is to apply such savings clauses.

One point not discussed in the opinion relates to the difference between non-compete and non-solicitation clauses. A non-compete clause typically prohibits a former employee from working in a job that competes with the employer's own products and services; virtually all courts require that such clauses be limited as to time (and often geographic area as well). But non-solicitation clauses simply prohibit the former employee from working for or trying to do business with the employer's customers and from trying to hire away the employer's other employees. Many courts have enforced non-solicitation clauses even though they did not contain time or geographic limitations.

In the MicroStrategy case, the court lumped non-compete clauses together with non-solicitation clauses and applied reasonableness requirements to both, without distinction.

Case references. *Motion Control Systems, Inc. v. East*, 546 S.E.2d 424 (Va. 2001); *Modern Environments, Inc. v. Stinnett*, 561 S.E.2d 694 (April 2002); *Mona Electric Group, Inc. v. Truland Service Corp.*, 193 F.Supp.2d 874 (E.D.Va. 2002), *aff'd*, 2003 WL 40748 (4th Cir. 2003); *MicroStrategy, Inc. v. Business Objects, S.A.*, 2002 WL 31678498 (W.D.Va. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 14.02.

Employers of Illegal Aliens Subject to Suit Under RICO

We know that all employees must, at time of hire, prove their eligibility to work in the U.S. by completing Form I-9 and exhibiting appropriate documentation to the employer. But it may come as a surprise that employers who hire undocumented workers may be classed as "racketeers" under the federal Racketeer Influenced and Corrupt Organizations Act (RICO).

Eastern Washington State is famous for its fruit orchards and also for its use of immigrant labor at harvest time. Two fruit companies, Zirkle and Matson, allegedly hired illegal aliens and paid them low wages, at least in part to depress the wages of all its workers, including documented workers. The companies allegedly could get away with paying low wages to illegals because their status made them vulnerable to exploitation.

Olivia Mendoza and Juana Mendiola, two *legal* employees of the fruit companies, brought a class action against their employers on the theory that the wage scheme amounted to racketeering under RICO.

RICO is a convoluted piece of legislation passed over 30 years ago to combat organized crime. It provides both criminal penalties and civil liability for persons who engage in a "pattern of racketeering activity" through an "enterprise." "Racketeering activity" is the commission of one of the numerous federal or state crimes listed in RICO, and a "pattern" of racketeering activity is committing two or more of those crimes. Among the listed crimes is "any act which is indictable under the Immigration and Nationality Act." An "enterprise" is basically any form of association.

Mendoza and Mendiola charged their employers with committing violations of the Immigration and Nationality Act as part of an enterprise to depress wages. As a result, they claimed, the Zirkle and Matson fruit companies were liable under RICO.

Although the federal district court in Washington dismissed Mendoza's and Mendiola's claim, the Ninth Circuit Court of Appeals reversed and sent the case back for trial. Without finding that Zirkle and Matson had in fact violated RICO, the Ninth Circuit said that Mendoza's and Mendiola's complaint, *if proved*, constituted a good claim under RICO.

The Washington fruit growers' case is similar to an earlier decision arising in Connecticut. In that case, a cleaning service company was allowed to bring a RICO action against a competitor for injuries allegedly flowing from the competitor's hiring of undocumented aliens in violation of federal immigration laws.

While these cases do not really change an employer's obligations when it comes to hiring undocumented workers, the cases do raise the stakes substantially: RICO provides for *treble* (triple) damages, just like the anti-trust laws, and RICO permits a successful plaintiff to recover his attorney fees.

Statutory references. 8 U.S.C. § 1324; 18 U.S.C. § 1961.

Case references. *Mendoza v. Zirkle Fruit Co.*, 301 F.3d 1163 (9th Cir. 2002); *Commercial Cleaning Services, LLC v. Colin Service Systems, Inc.*, 271 F.3d 374 (2d Cir. 2001).

EMPLOYER'S SURVIVAL GUIDE reference. 15.01.

"Unforeseeable Business Circumstances" Exception to WARN Act Obligations

The Worker Adjustment and Retraining Notification Act (WARN) requires employers with 100 or more employees to give 60 days' notice of plant closings and mass layoffs. A "mass layoff" is a layoff of at least 50 employees at a single site, which amounts to at least 33% of the employees at that site. However, the 60-day notice period is reduced or eliminated if the closing or layoff is "caused by business circumstances that are not reasonably foreseeable as of the time that the notice would have been required."

The question in a recent Sixth Circuit Court of Appeals case was whether the unforeseeable business circumstances exception applied to relieve a Michigan automobile parts plant of its WARN obligation.

Michigan Industrial Holdings (MIH) forged automobile parts for a company called Dana under written supply agreements. These agreements were renegotiated every year. One such agreement was due to expire on August 31, 1995, and at an August 25 meeting between MIH and Dana officials, Dana assured MIH the agreement would be renewed. In fact the agreement did not get renewed and MIH continued production for Dana on a month-to-month basis.

While discussions between MIH and Dana were ongoing, Dana was negotiating with another supplier. MIH was aware of those negotiations, but believed itself to be Dana's only viable supplier. Dana reassured MIH that this was so.

MIH and Dana operated on payment terms that required Dana to pay MIH within seven days of being invoiced. That arrangement was in place because of severe cash flow problems MIH was having. When one of Dana's weekly payments did not arrive, an MIH official called on Dana to pick up the check. It was then that Dana informed MIH it was not going to pay and it

would cease doing business with MIH. MIH was immediately forced to close its doors without giving the requisite 60-day notice under WARN.

In discussing the notice requirement, the Court quoted explanatory Department of Labor regulations –

> Advance notice provides workers and their families some transition time to adjust to the prospective loss of employment, to seek and obtain alternative jobs and, if necessary, to enter skill training or retraining that will allow these workers to successfully compete in the job market.

But WARN also recognizes that in some circumstances it may not be possible for employers to give the requisite notice. In deciding whether this so-called "unforeseeable business circumstances exception" is applicable, a court must evaluate whether a similarly situated employer, exercising commercially reasonable business judgment, would have foreseen the closing. So long as an employer is exercising reasonable business judgment, he will not be held liable under WARN for failing to predict economic conditions that may affect demand for his products or services.

In this case, said the Sixth Circuit, MIH's closing was the result of sudden and unexpected actions taken by Dana in refusing to make payment and in terminating its business relationship with MIH. Going back 60 days from that event, MIH was producing parts for Dana and could reasonably have believed it would continue doing so. Therefore, MIH's closing was unexpected and fell within the exception to WARN's notice requirement.

Statutory reference. 29 U.S.C. § 2101.

Regulatory reference. 20 C.F.R. § 639.

Case reference. *Watson v. Michigan Industrial Holdings, Inc.*, 2002 WL 31599919 (6th Cir. 2002).

***EMPLOYER'S SURVIVAL GUIDE* reference.** 19.09.

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In this issue of *Employer Alerts! ...*

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Employer Alerts!

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Infertility Treatment and the Pregnancy Discrimination Act

The Pregnancy Discrimination Act – an amendment to Title VII of the federal Civil Rights Act – defines sex discrimination to include discrimination because of pregnancy, childbirth, and related medical conditions. In the context of employer-sponsored group health insurance, the PDA requires that if a health plan provides comprehensive coverage for males, the plan must also provide equally comprehensive coverage for females. For example, a plan that includes a prescription drug benefit but excludes contraceptive drugs discriminates against women, since the vast majority of such drugs are designed for and taken by women. See "Contraceptive Coverage and Sex Discrimination," *Employer Alerts!,* Aug. 2001, p. 3.

A recent decision by the U.S. Court of Appeals for the Second Circuit (which sits in New York), ruled that an employer-sponsored group health insurance plan that excluded coverage for surgical impregnation procedures *does not* violate the PDA.

The plan provided benefits for a variety of infertility products and procedures, such as ovulation kits, oral fertility drugs, penile prosthetic implants and various other treatments. But it expressly excluded artificial insemination, in-vitro fertilization and embryo and fetal implants, all of which require surgery. Despite those exclusions, however, once pregnancy was achieved (whether through covered or excluded procedures) the plan covered all subsequent pregnancy-related expenses.

Employee Rochelle Saks, who participated in the plan, tried unsuccessfully to have a child with her husband. She underwent a number of different procedures, including surgical impregnation. When the plan denied benefits for the surgery, Saks sued, claiming sex discrimination in violation of the PDA. In support of her claim, she argued that while the plan provided complete coverage for surgical procedures that remedy infertility in men, it provided only incomplete coverage for female infertility.

The Court recognized that under the PDA, the proper inquiry in reviewing a sex discrimination challenge to an employer-sponsored group health insurance plan is (1) whether sex-specific medical conditions exist, and if so, (2) whether coverage exclusions for those medical conditions results in a plan that provides inferior coverage to one sex. In other words, equality is measured by the relative comprehensiveness of coverage for men and women.

Here, however, the plan did not discriminate against women.

First, the PDA was aimed at conditions that are unique to women, such as pregnancy and childbirth. Therefore, the PDA term "related medical conditions" must also be restricted to female-specific problems. Since infertility affects both men and women, a health plan may limit its infertility coverage without violating the PDA.

Second, the surgical impregnation procedures that Saks sought benefits for are used to address both male and female infertility. Surgical implantation might be appropriate in cases of male infertility or female infertility which, according to the Court, occurs at similar rates across genders. Because both genders are equally disadvantaged by exclusion of those procedures, the plan did not discriminate on the basis of sex.

Statutory reference. 42 U.S.C. § 2000e.

Case reference. *Saks v. Franklin Covey Co.*, 316 F.3d 337 (2d Cir. 2003).

Temporary Reassignment Not Fatal to FLSA Exempt Status

South Carolina Electric and Gas Company operates a nuclear power station in Jenkinsville, South Carolina. Every 18 months or so the plant is shut down for routine maintenance, during which the plant is refueled and other tasks are performed that cannot be accomplished while the plant is on-line. These shutdowns normally last 35 to 40 days.

To minimize downtime, the Company temporarily reassigns a number of employees to maintenance functions and it also asks employees to work overtime. Since maintenance work is considered to be nonexempt under the Fair Labor Standards Act, nonexempt employees who pull extra hours are paid time-and-a-half. However, as to employees who are normally classified as exempt, the Company does not pay time-and-a-half for overtime work while they are temporarily reassigned to reactor maintenance.

Some 17 administrative employees sued the Company for overtime. They admitted that under the Department of Labor's "short test," their normal jobs qualify them as exempt –

- they earn a salary of more than $250 per week;
- their primary duties consist of the performance of office or non-manual work directly related to management or general business operation; and
- they customarily and regularly exercise discretion and independent judgment.

The employees argued, however, that during the five weeks or so they were temporarily assigned to perform maintenance work, they should be reclassified as nonexempt and paid time-and-a-half for overtime. According to the employees, their status as exempt or nonexempt should be determined on a workweek-by-workweek basis.

The suit eventually went to the U.S. Court of Appeals for the Fourth Circuit (which covers Maryland and Virginia as well as the Carolinas). The Court ruled that since the short test looks to an employee's "primary duties," the entire 18-month plant maintenance cycle – not just the five weeks the employees were assigned to maintenance – should be considered. The five-week temporary assignment was insufficient, said the Court, to convert the employees from exempt to nonexempt.

The Court relied on an earlier case involving employees of Western Union. In that case, the Secretary of Labor tried to force Western Union to pay overtime to managerial employees who, during a strike, performed functions normally performed by nonexempt employees. The court there also rejected a workweek-by-workweek standard, ruling that the Western Union

managers retained their exempt status despite performing nonexempt, strike-breaking duties.

It should be noted that, had the employees here been paid between $155 and $250 per week, they would be subject to the Department of Labor's "long test," which considers additional factor in determining an employee's exempt status. The long test *does* take a workweek-by-workweek approach so that, had the long test been applicable here, these employees would have been nonexempt and entitled to overtime for the five weeks they were assigned to plant maintenance.

Statutory reference. 29 U.S.C. § 207.

Regulatory reference. 29 C.F.R. § 541.2.

Case references. *Counts v. South Carolina Electric & Gas Co.*, 317 F.3d 453 (4th Cir. 2003); *Marshall v. Western Union Telegraph Co.*, 621 F.2d 1246 (3d Cir. 1980).

FLSA's "Window of Correction"

In another Fair Labor Standards Act case, the U.S. Court of Appeals for the Fifth Circuit ruled that an employer who makes improper salary deductions that trigger loss of exemption may refund the deductions with interest and protect the employees' exempt status.

In order for an executive, administrative or professional employee to qualify for exemption under FLSA's overtime requirements, the employee must be "salaried." So if an employer treats an otherwise exempt employee as if he were hourly, then the employee will lose his exempt status. For example, docking an employee's pay for being tardy, or while on jury duty, or when no work is available, amounts to treating that employee as an hourly worker. See "Exempt Employees and the 'Salary Basis' Requirement," *Employer Alerts!*, Apr. 2001, p. 1.

Suppose an employer improperly withholds pay from an employee and, while that deduction policy is in effect, the employee works overtime. Is the employee entitled to time-and-a-half? Can the employer correct the deduction and avoid paying overtime?

Department of Labor regulations provide –

> The effect of making a deduction ... when there is no work available, ... indicates that there was no intention to pay the employee on a salary basis. In such a case the exemption would not be applicable to him during the entire period when such deductions were being made. On the other hand, where a deduction not permitted by these [regulations] is inadvertent, or is made for reasons other than lack of work, the exemption will not be considered to have been lost *if the employer reimburses the employee for such deductions and promises to comply in the future.*

A recent case illustrates how this so-called "window of correction" works.

Hannon Food Service owns a number of KFC restaurants in Mississippi, each of which is run by a supervising manager. Hannon pays each manager a base weekly salary of $300, plus a weekly bonus equal to 2% of gross sales from the particular restaurant where the manager works. Hannon considers its managers as exempt for FLSA overtime purposes.

Hannon had a policy of deducting recurrent cash register shortages from its managers' monthly bonuses. Deductions from *bonuses* did not affect exempt status because the managers qualify as exempt on their base salaries. (Under FLSA, it is permissible to vary a portion of an exempt employee's pay to reflect quality or quantity or work, so long as the employee's compensation includes a fixed component which does not vary based on hours worked, productivity, etc.)

In an effort to reduce cash register shortages, Hannon changed its policy and began deducting shortages from its managers' *base salaries*. The new policy *did* affect the managers' exempt status because it amounted to treating them as hourly workers, not salaried employees.

Some four months after the new policy had been in place, Hannon informed its legal counsel about the practice. Counsel advised Hannon to discontinue the practice and Hannon promptly did so, reverting to its earlier policy of docking only bonus payments for cash register shortages. In the meantime, the managers worked substantial overtime, for which they made claim.

Five days before the managers' claims were due to be tried in court, Hannon offered to refund the improper deductions along with 8% interest. The managers rejected the offer and demanded their overtime, arguing that since the improper deductions took place over a four-month period they were hardly inadvertent and therefore could not qualify for the window of correction.

The Fifth Circuit (which hears federal appeals from Texas, Mississippi and Louisiana) disagreed and denied the managers' overtime claims. According to the Court, the plain language of DOL's regulations sets out "inadvertence" and "made for reasons other than lack of work" as *alternative* grounds for permitting corrective action. Since the improper deductions here were not made for lack of work, the window of correction was available whether or not the deductions were inadvertent.

Hannon properly availed itself of the window of correction, said the Court, by tendering back the improper deductions, with interest, five days before trial. Reimbursements may be made at any time to preserve the window of correction.

Statutory reference. 29 U.S.C. § 216.

Regulatory reference. 29 C.F.R. § 541.118

Case reference. *Moore v. Hannon Food Service, Inc.*, 317 F.3d 489 (5th Cir. 2003).

Discrimination and the "Same Actor/Same Group" Inferences

The "same actor" inference postulates that when a supervisor who *fires* an employee is also the same supervisor who originally *hired* the employee, the firing cannot be discriminatory. In other words, if the supervisor were going to discriminate on the basis of the employee's race, sex, age, etc., he wouldn't have hired the employee in the first place, so the subsequent firing must have been for reasons other than discrimination.

The "same group" inference says that when the supervisor is a member of the same racial, gender or age group as the fired employee, there could be no discrimination, because members of the same group don't discriminate against each other.

Neither inference fared well in a recent decision of the U.S. Court of Appeals for the Sixth Circuit (which hears federal appeals from Kentucky, Michigan, Ohio and Tennessee). Although the case dealt with age discrimination under the Age Discrimination in Employment Act, its ruling is equally applicable to other forms of discrimination prohibited by federal law.

Donald Wexler was hired as a salesman by Gordon Shiffman, president and majority owner of White's Fine Furniture. At the time, Wexler was 55 years old and Shiffman was in his mid-sixties. After about two years, Shiffman promoted Wexler to manager of one of White's stores. In the face of declining sales at the store, however, Shiffman later demoted Wexler back to salesman.

Shiffman himself, as well as other corporate officers, had made numerous adverse comments about

his age. After Wexler's demotion, the manager's position was filled by a person in his early 30's.

Wexler brought an age discrimination claim against White's Fine Furniture, citing Shiffman's and other's repeated references to Wexler's age. The lower court dismissed Wexler's suit, relying in part on the same actor inference and the same group inference. On appeal, however, the case was reinstated and sent back to the lower court for trial.

According to the appellate court, Wexler's evidence indicated that age was at least a factor in Shiffman's decision to demote him. Neither the same actor inference nor the same group inference was sufficient, said the Court, to overcome Wexler's evidence and justify summary dismissal of the case. In situations like this, where there is evidence of discrimination on the one hand, and same actor or same group inferences on the other hand, the case must go to trial.

The Court's conclusion as to the same group inference appears consistent with the law generally. For example, the Supreme Court held in 1998 that male "roustabouts" on an oil drilling platform in the Gulf of Mexico who sexually harassed another male were guilty of sex discrimination. Similarly, a black security guard at a Nebraska prison committed race discrimination when he reassigned a black subordinate in retaliation for a discrimination grievance the subordinate had filed. See "Members of 'Protected Classes' Can Discriminate, Too!," *Employer Alerts!*, March 2001, p. 5.

But courts elsewhere have reached a different conclusion about the weight to be given the same actor inference. In the Fourth Circuit for example, the inference has been called "strong" and "powerful," justifying prompt dismissal of discrimination claims when the hirer and firer are the same person and the hiring and firing take place within a relatively short time. Quoting a law review article, the Fourth Circuit said in 1991 –

> Claims that employer animus exists in termination but not in hiring seem irrational. From the standpoint of the putative discriminator, it hardly makes sense to hire workers from a group one dislikes (thereby incurring the psychological costs of associating with them), only to fire them once they are on the job.

Statutory reference. 29 U.S.C. § 621.

Case reference. *Wexler v. White's Furniture, Inc.*, 317 F.3d 564 (6th Cir. 2003) (*en banc*); *Oncale v. Sundowner Offshore Services, Inc.*, 523 U.S. 75 (1998); *Ross v. Douglas County, Nebraska*, 234 F.3d 391 (8th Cir. 2000); *Proud v. Stone*, 945 F.2d 796 (4th Cir. 1991).

Delay in Offering Accommodation Violates Maryland Disability Law

Susan Cohen was a full-time social worker with the Montgomery County Department of Health and Human Services. She had worked there for over 20 years when she was diagnosed with multiple sclerosis. As the disease progressed she suffered increased weakness in her upper and lower extremities, which interfered with her ability to drive and write. That in turn limited her ability to do field visits with the Department's clients and to use a computer for long periods.

Cohen asked the Department for reasonable accommodation of her disability by restructuring her job or reassigning her. According to her complaint, however, the Department delayed for over 17 months in dealing appropriately with her situation. But by the time she filed suit, she had been accommodated.

The trial court dismissed Cohen's suit, reasoning that her claims were now moot since she been reassigned as requested. The Court of Special Appeals disagreed, ruling that unreasonable delay makes an

otherwise reasonable accommodation unreasonable. In the Court's words, "accommodation delayed is accommodation denied." To hold otherwise, said the Court, would reward dilatory tactics and discourage disabled employees from requesting accommodations in the first place.

Equally significant was the appellate court's ruling that Cohen could sue two individual County employees – John Kenney, chief of the County's Aging and Disability Services, and Judith Unger, administrator of the County's Human Resources Department – on the basis that they were personally responsible for the discrimination she suffered. It remains to be seen what if any relief Cohen will obtain against the individuals.

Statutory reference. Md. Code, Art. 49B, § 14; Mont. Cnty. Code, § 27-19.

Case reference. *Cohen v. Montgomery County*, 2003 WL 548853 (Md.App. No. 2344, decided Feb. 27, 2003).

Do Females Have Constitutional Right to Wear Skirts?

Constitutional guarantees, such as due process, equal protection, and freedom of speech, generally apply only to government, not private, employment. Nevertheless, a recent decision by the Second Circuit in New York is worthy of mention.

The Sullivan County New York transit authority adopted a dress code which required all driver employees to wear uniforms. The prescribed uniform included pants, but no skirts. The stated purpose of the dress code was "to encourage customers to be more respectful of the drivers, to foster a positive esprit-de-corps among drivers and to project an overall positive appearance for the County."

Grazyna Zalewska, a van driver for the County, asked her supervisor for an exception to the rule, explaining that she had never worn pants in her life and that doing so would be contrary to deeply held cultural values. The supervisor denied Zalewska's request, saying no exceptions would be made, consistent with the County's view that "pants are safer than skirts for the operators of vans, particularly vans with chair lifts, as the operator must assist customers on and off the vehicle."

When Zalewska went to the County's private uniform vendor to get her uniform, she managed to convince the vendor to furnish her with a skirt instead of pants. Zalewska worked in her customized uniform for several weeks without incident, but eventually her supervisor ordered her to wear pants. When she refused, she was suspended and then transferred to another department.

Zalewska sued the County, claiming its skirt requirement and subsequent disciplinary action against her violated her First Amendment free speech rights under the Constitution, and her due process and equal protection rights under the Fifth and Fourteenth Amendments.

The Second Circuit rejected Zalewska's free speech claim, relying on earlier Supreme Court precedent that dress and grooming codes don't amount to "speech," unlike black arm bands, for example, which were protected speech in protest of the Vietnam war.

The pants-only dress code also survived Zalewska's other challenges. While one's dress and personal appearance can implicate due process and equal protection rights, here the County's rule was sufficiently rational to satisfy constitutional requirements.

Although the Court observed that the County's policy was gender neutral and without discriminatory intent, it appears from the decision that Zalewska never really pushed a discrimination claim. Had she done so, the result here might have been different.

At least for the time being, however, if you what to be a van driver in Sullivan County, New York, you'd better be prepared to zip up.

Case reference. *Zalewska v. County of Sullivan*, 316 F.3d 314 (2d Cir. 2003).

FMLA Changes May Be in the Works

Congress is continually tinkering with the Family and Medical Leave Act, although none of its proposed changes have made it into law so far. But a recent bill, introduced by Sen. Christopher Dodd (D-Conn.) deserves watching.

Under FMLA, an employer with 50 or more employees must offer unpaid leave of up to 12 weeks to an eligible employee for the birth or adoption of a child, if the employee has a serious health condition, or to care for a spouse, child or parent with a serious health condition. The employer also must continue health insurance coverage during leave without additional cost to the employee.

The new proposal would reduce the 50-employee threshold to 25, significantly expanding the number of employers covered by the law. The proposal would also create a pilot grant program to help states design ways to offer partial or full pay for six of the 12 weeks an employee is on FLMA leave.

Watch this space for updates on the bill's progress.

Statutory reference. 29 U.S.C. § 2601; S. 304 (108th Cong., 1st Sess.).

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In this issue of *Employer Alerts! ...*

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Employer Alerts!

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Outer Limits of Reasonable Accommodation Under the ADA

The Americans with Disabilities Act requires an employer to reasonably accommodate an individual who suffers an impairment that substantially limits one or more major life activities, so long as the individual will then be able to perform all the essential functions of his or her job.

What is "reasonable" in this context? The ADA itself gives some examples. For one, the employer's facilities must be readily accessible and usable. Wheel chair ramps may have to be installed and doorways and restroom facilities may need to be enlarged. Other examples *might* include –

- restructuring jobs;
- modifying work schedules;
- relaxing workplace rules;
- making reassignments to vacant positions; and
- modifying equipment.

The list of what's reasonable goes on. But it is not limitless. Two recent cases provide good examples of its outer bounds.

Indefinite Leave Not Reasonable

Mark Wood started working for the Clerk's Office of the Lee County, Florida Circuit Court in 1974. In 1978 he began suffering from cluster headaches and, by 1985, his condition caused him to miss lengthy periods of work. The headaches also prevented him from completing a substantial portion of his duties.

The Clerk's Office was generous with Wood, routinely extending him discretionary leave when he had exhausted vacation and sick leave. The Office even created a new position for him in an effort to work around his frequent absences. Still, the headaches persisted and Wood continued to take substantial time off. In 1995, for example, he missed a total of seven weeks' work, and in 1998 he was out approximately 15 weeks.

The year 1999 was even worse for Wood. By December of that year, Wood asked for additional leave (supported by a letter from his physician), but could promise no specific return date. In early January, while

still on leave, Wood was fired.

Wood sued under the ADA and his case eventually reached the Eleventh Circuit U.S. Court of Appeals. The Court upheld Wood's dismissal, saying that indefinite leave is not a reasonable accommodation. While a leave of absence might be reasonable in some circumstances, nothing in the ADA requires an employer to wait an indefinite period for an accommodation to achieve its intended effect.

According to the Court, the ADA covers people who can perform the essential functions of their job presently or in the immediate future. Since Wood could not perform his job, his employer had no obligation to grant him indefinite leave on the hope that, sometime in the future, Wood might be able to work.

Full-Time Home Office Not Reasonable

Beverly Rauen rose from secretary to software engineer at United States Tobacco, obtaining her college degree under UST's tuition reimbursement program. She did her job exceedingly well and actually performed duties above and beyond her position.

Unfortunately, Rauen suffered several bouts with cancer, the treatment for which took a serious toll. Because she had lost a section of her small intestine, she was required to take IV fluids on a daily basis. This in turn necessitated frequent bathroom visits. In addition, she was easily fatigued and needed to rest during the day. Despite her condition, however, she continued to perform her job at a high level of proficiency.

In January 1999 Rauen presented UST with a letter from her doctor stating that it would be beneficial for her to work from a home office. In response, UST requested Rauen to sign a medical release that would enable UST's consulting physician to review her medical records and evaluate the request. Rauen refused to give the release because, according to her, the physician also held a law degree and she was uncomfortable giving her medical records to a UST lawyer.

No further action was taken on Rauen's January 1999 home office request, and she continued to work full-time as before.

In May 1999, Rauen renewed her request to be allowed to work from home. UST agreed to meet with her to discuss the possible accommodation, even though she had never signed a medical release. A meeting did take place and Rauen made clear that what she wanted was to work at home on a full-time basis and come into the office when and if *she* determined her presence at the office was necessary. UST made a number of suggestions short of full-time work at home, such as scheduling a regular day each week when Rauen would come to the office, but Rauen rejected those suggestions. As the Court later put it –

> [T]he accommodation Rauen sought was a home office 'in its entirety.' According to her, she would accept nothing less than being allowed to work from home when she thought she was not needed in the office.

Nothing came of the meeting and eventually Rauen filed suit, claiming that UST had failed to reasonably accommodate her under the ADA. All the while, she continued to work in her usual manner at UST's office.

The U.S. Court of Appeals for the Seventh Circuit rejected her suit. The Court said that, generally speaking, an employer is not required to accommodate a disability by allowing the disabled worker to work by himself, without supervision, at home. The reason is that most jobs require the kind of teamwork, personal interaction and supervision that simply cannot be performed at home without compromising the quality of the employee's performance.

While there may be exceptions to the rule against a work-at-home accommodation, said the Court, it would take a "very extraordinary case" to require such an accommodation from an employer. Rauen's case did not rise to that level.

As an interesting aside, the Court also pointed out that Rauen was in fact able to perform all the essential elements of her job – and do them extremely well – without any accommodation at all. Why then, asked the Court, was any accommodation (no less an unreasonable one such as working at home) even required?

Statutory reference. 42 U.S.C. § 12101.

Case references. *Wood v. Green*, 2003 WL 1090412 (11th Cir. 2003); *Rauen v. United States Tobacco Mfg. L.P.*, 2003 WL 262477 (7th Cir. 2003).

How Young Is Too Young Under the ADEA?

The Age Discrimination in Employment Act prohibits discrimination against persons 40 years of age or older on the basis of age. So if a 55-year-old is fired because of his age, he has a good claim under the Act.

Of course, the worker still has to *prove* that he was fired due to age. He'll have an easy time doing that if his boss said, in front of witnesses, "I'm letting you go because you're just too old for the job." But it's often hard to find such direct evidence of discriminatory motive. In the more usual case, the boss's motive is unclear (or at least unexpressed) and circumstantial evidence is all that's available.

One type of circumstantial evidence is an age differential between the person fired and the person hired to replace him. If the replacement for a 55-year-old is a mere 35, that provides some evidence of age discrimination. But what if the replacement is 40 years old instead of 35? In other words, does the replacement need to come from *outside* the protected class to prove a circumstantial case of age discrimination?

Some six years ago the Supreme was faced with that very question. The Court said –

> The fact that one person in the protected class has lost out to another person in the protected class is ... irrelevant, so long as he has lost out *because of his age*.

So in the example above, the fired 55-year-old can make out a circumstantial case under the ADA even if his replacement is within the 40-plus protected class himself.

But the Supreme Court said something else of interest –

> In the age-discrimination context, ... an inference [of illegal discrimination] cannot be drawn from the replacement of one worker with another worker [who is] *insignificantly younger*.

So if the 55-year-old were replaced by someone who was, say, 54 years old, the age difference, being insignificant, would not amount to a circumstantial case of age discrimination.

The Supreme Court did not say what in its view would be a significant age difference, and the lower courts have come up with a variety of answers ranging from three years to ten. Now the Massachusetts Supreme Court, applying the Commonwealth's own age discrimination law, has come up with an answer of its own.

After reviewing a number of other court decisions, the Massachusetts Court has said it will set the age difference in that state at *five* years. The Court –

> recognize[d] that a line has to be drawn somewhere. Otherwise, the byproduct of an essentially undefined standard could be inconsistent and possibly capricious jury verdicts with a lack of predictability .... We conclude that an age disparity of less than five years, by itself, is too insignificant.

The "by itself" qualification in the Court's decision should be noted. If an employee is replaced by a younger person where the age difference is *less than* five years, but the employee has *other evidence* of age discrimination, then the employee could still prevail in court.

Statutory reference. 29 U.S.C. § 621.

Case references. *O'Connor v. Consolidated Coin Caterers Corp.*, 517 U.S. 308 (1996); *Knight v. Avon Products, Inc.*, 438 Mass. 413 (2003).

Failure to Get More Prestigious Title Not Adverse Action for Discrimination Purposes

Title VII prohibits discrimination in hiring, firing, compensation, and other "terms," "conditions" and "privileges" of employment. What are "terms," "conditions" and "privileges" of employment? Ready examples include shift assignments, fringe benefits such as vacation, sick leave, insurance programs, and access to facilities like the cafeteria and fitness center. Even the intangible "work environment" is covered by Title VII, so an employer who tolerates a workplace filled with demeaning racial or sexual slurs can be sued by the target of those slurs and by others who find the environment offensive.

But trivial or inconsequential workplace actions by the employer will not support a Title VII action. When does an action rise above the trivial or inconsequential and qualify as adverse? The Supreme Court has said that a job action must amount to a "significant change in employment status." The action must also be objectively detrimental, not just something a particular employee dislikes. As another court put it, not everything that makes an employee unhappy is an actionable adverse action, nor are changes that make a job less appealing but that do not affect a term, condition or benefit of employment.

A recent decision by the U.S. Court of Appeals for the Seventh Circuit illustrates.

Mickey Grayson, an African-American, was a carpenter for the City of Chicago. He had over 25 years of experience as a journeyman carpenter. At the time the City posted three new job openings – General Foreman, General Foremen of Carpenters, and Foreman of Carpenters – he had risen to the level of Subforeman.

Grayson applied and was interviewed for the three positions, but did not get any of them. Instead, the City hired three white candidates. Each of the white candidates had actually been holding the respective new positions on an "acting" basis for several years and, according to the City, had more relevant experience than Grayson.

Although Grayson lacked any direct evidence of racial discrimination, he decided to sue the City. In ruling against him, the Seventh Circuit concluded that he was simply not in the same situation as the two candidates who got the General Foreman and General Foremen of Carpenters positions. In each case, the successful candidate did in fact have more relevant experience.

With respect to the Foreman of Carpenters position, Grayson and the successful white candidate had similar experience and qualifications. But because Grayson's existing position of Sub-foreman was identical in all but title to Foreman of Carpenters, Grayson's rejection did not amount to a materially adverse employment action. Denial of a loftier title, said the Court, where salary, benefits and responsibility would have been unchanged, is not a violation of Title VII.

Statutory reference. 42 U.S.C. § 2000e.

Case references. *Burlington Industries, Inc. v. Ellerth*, 118 S.Ct. 2257 (1998); *Brown v. Brody*, 199 F.3d 233 (D.C.Cir. 1999); *Russell v. Principi*, 257

F.3d 815 (D.C.Cir. 2001); *Grayson v. City of Chicago*, 317 F.3d 745 (7th Cir. 2002).

Are Shareholders and Partners "Employees" for Discrimination Purposes?

Title VII and other federal discrimination laws apply only to employers who meet specified thresholds. Title VII, for example, requires the employer to have 15 or more employees before he can be sued under that law. If the threshold is not met, neither the courts nor the EEOC has jurisdiction to hear a Title VII suit. See "Bordello Wins Title VII Case Thanks to Poor Record-keeping," *Employer Alerts!*, Oct. 2002, p. 6. (State and local anti-discrimination laws often have lower thresholds, so an employer isn't necessarily free to discriminate just because federal law doesn't apply.)

And, of course, only an "employee" can bring a Title VII suit.

The determination of who is and who is not an employee has been a matter of some dispute. The discrimination laws themselves are not at all helpful. They typically define "employee" in circular fashion as "an individual employed by an employer."

In a 1997 Supreme Court case, the employer had between 15 and 17 employees on its payroll, but at various times it was not actually compensating 15 or more employees. The difference resulted from the fact that two of its employees were part-time who worked fewer than five days per week. The Court ruled that the employer was subject to Title VII, adopting what has become known as the "payroll method" for counting employees. Under that method, if an employee appears on the employer's payroll, he is counted whether or not he is actually being compensated on a particular day. In short, part-time as well as full-time employees count.

The question also arises regarding shareholders of small business corporations or partners in professional practices. Even though they work for the business, just like regular employees, they also own and manage the business.

Last year, the EEOC attempted to enforce an investigatory subpoena against a large Chicago-based law firm. The investigation related to the firm's demotion of some 32 lawyers, possibly in violation of age discrimination laws. The firm resisted the subpoena on the ground that the demoted lawyers were partners, not employees, so the demotions could not give rise to discrimination claims. The Seventh Circuit enforced the subpoena anyway, saying that at least at the investigative stage, there was continuing doubt over whether the 32 lawyers should be deemed bona fide partners (and thus employ*ers*), or de facto employ*ees*.

Just this past month the Seventh Circuit applied what is called an "economic realities test" in deciding that a shareholder in a medical practice could not sue his own corporation for age discrimination. In so ruling, the Court disregarded the shareholder's status as an employee for state law purposes and looked instead to his participation in the management and control of the corporation.

While the Seventh Circuit's decision is certainly defensible, other circuit courts reject the "economic realities test" and reach a different conclusion.

It is curious that the Seventh Circuit issued a decision at this time. A closely related question, of whether shareholders of in a medical practice count in determining Title VII's 15-employee threshold, is now pending before the Supreme Court; a decision is expected before the summer.

Case references. *Walters v. Metropolitan Educational Enterprises, Inc.*, 519 U.S. 202 (1997); *Stinnett v. Iron Works Gym*, 2002 WL 1962138 (7th Cir. 2002); *Clackamas Gastroenterology Associates, P.C. v. Wells*, 271 F.3d 903 (9th Cir. 2001), *cert.*

granted, 123 S.Ct. 31 (2002); *Schmidt v. Ottawa Medical Center, P.C.*, 2003 WL 730080 (7th Cir. 2003); *EEOC v. Sidley, Austin, Brown & Wood*, 315 F.3d 696 (7th Cir. 2002).

Employee's Duty of Loyalty in Virginia

While employees owe a duty of loyalty to their employers, in the absence of a non-compete or similar agreement the duty ends upon termination of employment. Further, employees may make preparations to compete even before their employment ends, so long as they don't actually begin competing. A pair of recent Virginia cases helps draw the line between preparations and actual competition.

Williams v. Dominion Technology

Dominion Technology Partners, based in Chesterfield County, specializes in recruiting computer consultants and placing them, either directly or through a broker, with companies in need of such expertise. When Dominion learned that the power tool company Stihl needed a consultant to oversee installation of a new software package at Stihl's facilities in Virginia Beach, Dominion recruited Donald Williams as a candidate.

Dominion offered to pay Williams $80 per hour on an at-will basis and Williams agreed. Williams was not required to sign any non-compete or other agreements connected with his new employment.

After recruiting Williams, Dominion referred him to Stihl for an interview, and Stihl found him satisfactory. At that point, for reasons not explained in the court opinion, Dominion entered into a contract with an employment brokerage firm named ACSYS Information Technology and ACSYS, in turn, contracted with Stihl for Williams' services. Under these arrangements, Stihl paid ACSYS $165 per hour for Williams' services, ACSYS paid Dominion $115, and Dominion paid Williams $80.

As the initial project at Stihl neared completion, Williams learned that Stihl was considering a further software upgrade. He also learned that Stihl was paying $165 for his work, only $80 of which reached him. So Williams contacted ACSYS, saying he wanted to end his relationship with Dominion, but would be willing to work through ACSYS in providing further services to Stihl. ACSYS agreed to this new arrangement and began paying Williams $115 per hour instead of the $80 he had been making at Dominion.

When Dominion found out that Williams was continuing to provide consulting services to Stihl, Dominion sued Williams. Its suit claimed a variety of wrongs, including breach of contract, tortious interference with business relationships, and breach of fiduciary duty.

Eventually the suit reached the Virginia Supreme Court. The Court recognized that an employee, including an at-will employee, owes a duty of loyalty to his employer, including specifically a duty not to compete with his employer during the employment. On the other hand, in the absence of covenants governing post-employment conduct, an employee has the right to make arrangements during his employment to compete after resigning his post.

Here, Williams would have been perfectly free to leave Dominion and *then* contact ACSYS about continued work for Stihl. But the question in this case was whether Williams could contact ACSYS *while still employed* by Dominion. The Virginia Supreme Court answered that question in Williams' favor and rejected Dominion's suit.

The Court pointed out that just because an employee's conduct causes harm to his employer, that does not automatically make the conduct wrongful. As the Court said, "The law will not provide relief to every disgruntled player in the rough-and-tumble world comprising the competitive market place." In addition, Dominion could easily have protected itself with a reasonable non-compete or non-solicitation agreement.

Finally, Stihl's need for additional consulting services was no more than a lead; it did not amount to a Dominion trade secret entitled to court protection.

Advanté Designs v. McGinnis

In this case, decided by the Circuit Court for the City of Richmond, David McGinnis managed the pre-press and print division of Advanté Designs. Advanté had previously done design work for the Republican Party, but when the Party contacted McGinnis in 1999 for additional work, McGinnis referred the customer to McGinnis' wife, who had her own graphic design business. Worse, McGinnis allowed his wife to use Advanté's facilities to do her work, all without informing Advanté or sharing any revenue with Advanté.

Later, McGinnis himself used Advanté's facilities to perform some $350,000 worth of work for a customer, again without informing Advanté or sharing any of the revenue.

In 2001, McGinnis resigned from Advanté and hired away a number of Advanté's employees for a new business McGinnis had formed. That new business earned more than $2 million in revenues over a two-year period from one of Advanté's former customers.

The Circuit Court had little trouble holding McGinnis liable for breach of his duty of loyalty. The Court said –

> An employer has a right to expect that its employees will perform under the terms of the employment contract to benefit the employer. The employer is entitled to all the profits derived as a result of the employee's efforts during the course of employment. In fact, the employer is deemed to have property rights in those profits.

Accordingly, the Court awarded Advanté almost $950,000 in compensatory damages and an additional $10,000 in punitive damages.

Case references. *Williams v. Dominion Technology Partners, LLC*, 2003 WL 722824 (Va. 2003); *Advanté Designs, Inc. v. McGinnis* (Richmond Va. Cir. No. LP-462-1, 2003).

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In this issue of *Employer Alerts! ...*

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Supreme Court Lists Factors for Setting Employment Status of Shareholder-Directors Under ADA

Just last month we reported on several cases dealing with whether owner-employees should be counted as employers or employees under federal anti-discrimination laws. See "Are Shareholders and Partners 'Employees' for Discrimination Purposes," *Employer Alerts!*, April 2003, p. 5. The Supreme Court has now answered the question – sort of.

The case involved an Oregon medical clinic that was sued for disability discrimination by the clinic's bookkeeper. The bookkeeper argued that the clinic met the 15-employee threshold for bringing an ADA claim so long as four of its physician-shareholders were counted. She pointed out, for example, that the physician-shareholders had employment contracts, they were salaried, and they were treated as employees for tax purposes. The clinic claimed otherwise – that the physician-shareholders were really more like partners in a partnership and should therefore not be counted.

The Court itself emphasized that the physician-shareholders are employees for pension plan purposes under ERISA, which was the prime reason they chose a corporate, rather than a partnership, form. But in the end, the Court rejected simple analogies to corporations and partnerships. Instead, the Court ruled that common law principles should be applied.

Citing EEOC regulations, the Court listed six factors to be considered in determining whether a shareholder-director of a professional corporation is an employee for discrimination purposes –

- Whether the organization can hire or fire the individual or set the rules and regulations of the individual's work;
- Whether, and if so, to what extent the organization supervises the individual's work;
- Whether the individual reports to someone higher in the organization;
- Whether and, if so, to what extent the individual is able to influence the organization;
- Whether the parties intended that the individual be an employee, as expressed in written agreements or contracts; and

! Whether the individual shares in the profits, losses, and liabilities of the organization.

Although the case arose under the Americans with Disabilities Act, it seems safe to assume that the Court's approach will be applicable to other federal anti-discrimination laws, such as Title VII (discrimination on the basis of race, religion, sex, etc.) and the ADEA (age discrimination).

Whatever the merits of this decision, the six factors the Supreme Court said must be considered are highly fact-specific. This results in even less certainty for employer and employee alike and an increase in costs and delays for discrimination lawsuits.

Case reference. *Clackamas Gastroenterology Associates, P.C. v. Wells*, 2003 WL 1906297 (U.S. 2003).

Firing for Misconduct Upheld Despite FMLA Leave

The Family and Medical Leave Act requires employers with 50 or more employees to grant up to 12 weeks of leave without pay to eligible employees for the birth or adoption of a child, if the employee has a serious health condition, or to care for a spouse, child or parent with a serious health condition. The employer also must continue health insurance coverage during leave without additional cost to the employee.

When an employee returns to work after being on FMLA leave, he is entitled to return to the same position he held before taking leave, or to an equivalent position. And of course the employer cannot discriminate or retaliate against an employee for having taken FMLA leave.

So when Viengsamon Pharakhone was fired by Nissan North America after expiration of his FMLA leave, he sued.

Pharakhone showed in his suit that he had approached his supervisor and explained that his wife was expecting, that she would be delivering within the month, and that he needed some time off. When the baby did arrive, Pharakhone called his supervisor and asked for four weeks' leave, which the supervisor approved.

It turned out that one of the reasons Pharakhone needed leave was to fill in as manager of his wife's restaurant while she tended to their newborn child. Although Nissan had a strict policy against an employee's performing any outside work while on leave, Pharakhone worked as restaurant manager anyway. When Nissan discovered that Pharakhone was working while on leave, it fired him for violating company policy.

The U.S. Court of Appeals for the Sixth Circuit (which covers Kentucky, Michigan, Ohio and Tennessee) upheld the termination. The Court pointed out that the right to reinstatement is not absolute, since an employer need not reinstate an employee who would have lost his job even if he had not taken FLMA leave. Because Pharakhone was fired for violating a company policy unrelated to FMLA, he could not claim protection under that statute.

In upholding Pharakhone's firing, the Sixth Circuit relied on the Department of Labor's FMLA regulations. Those regs list a number of circumstances under which an employer may refuse to reinstate or delay reinstatement –

! If an employee fails to provide a requested fitness-for-duty certification to return to work, an employer may delay restoration until the employee submits the certificate.

! An employee has no greater right to reinstatement or to other benefits and conditions of employment than if the employee had been continuously employed during the FMLA leave period.

! An employer may require an employee on FMLA

leave to report periodically on the employee's status and intention to return to work.

! An employee who fraudulently obtains FMLA leave from an employer is not protected by FMLA's job restoration or maintenance of health benefits provisions.

! If the employer has a uniformly-applied policy governing outside or supplemental employment, such a policy may continue to apply to an employee while on FMLA leave.

Misconduct that occurs *before* FMLA leave can also justify discipline *while* an employee is out on leave. In other words, FMLA does not require an employer to suspend its normal policies just because an employee has qualified for leave. See "Disciplinary Action Against Employee on FMLA Leave," *Employer Alerts!*, May 2001, p. 4. As reported in that article, a police department was not prevented from going forward with a disciplinary hearing against one of its officers accused of misconduct, even though the hearing occurred while he was on FMLA leave.

Statutory reference. 29 U.S.C. § 2601.

Regulatory reference. 29 C.F.R. § 825.312.

Case references. *Pharakhone v. Nissan North America, Inc.*, 2003 WL 1720092 (6th Cir. 2003); *Coleman v. Anne Arundel County Police Dept*., 766 A.2d 169 (Md. App. 2001), *aff'd*, 797 A.2d 770 (Md. 2002).

Late Notice Bars Insurance Coverage for Sex Harassment

In the February issue of *Employer Alerts!* we recommended that one of the steps an employer take to avoid sexual harassment liability is to check the notice provisions of his Employment Practices Liability Insurance policy. See "Training as Additional Element of Sexual Harassment Defense," *Employer Alerts!*, Feb. 2003, p. 1. Here's why.

Interstate Cleaning Corp. (ICC), headquartered in Missouri, provides cleaning services to shopping malls, retail stores and commercial buildings throughout the U.S. Commercial Underwriters Insurance Company insured ICC under a general commercial liability insurance policy that apparently included coverage for employment-related matters. The policy required ICC to give "immediate" notice to the insurance company of any claim made or suit brought against ICC. The policy had a $50,000 self-insurance provision, meaning that ICC was responsible for the first $50,000 in losses, but the immediate notice requirement still applied even if the claim or suit was within ICC's self-insurance limit.

ICC employed Chad and Jamie Awai in Hawaii. In May 1997, the Awais informed ICC that they had been subjected to sexual harassment by their supervisor. Five months later, the Awais sued ICC in Hawaii.

Believing the Awais' action to be a nuisance suit, ICC decided to handle the matter itself and not notify the insurance company. When the Awais offered to settle for $25,000, ICC said no and insisted on going to trial. The Awais won at trial, but the court ordered a retrial on the ground that the jury verdict was excessive. The Awais appealed that order and, while the case was on appeal, ICC and the Awais reached a settlement of the case.

Only then, some two years after the Awais first made claim, did ICC notify the insurance company. Not surprisingly, the company denied liability based on the late notice. So ICC sued its insurance carrier in Missouri federal court.

The case eventually reached the U.S. Court of Appeals for the Eighth Circuit, which ruled in favor of the insurance company. The Court first concluded that late notice alone would not defeat an insurance claim

because, under Missouri law, the insurance company must show that it had been prejudiced by the delay. (Maryland has a similar rule, but no showing of prejudice is required in Virginia and the District.) Here, however, it was obvious that the insurance company was prejudiced, because the company was deprived of any opportunity to investigate the facts surrounding the Awais' claim, to defend on liability, to settle the suit, or to choose a trial strategy.

Statutory reference. Md. Code, Ins. § 19-110

Case references. *Interstate Cleaning Corp. v. Commercial Underwriters Ins. Co.*, 2003 WL 1884226 (8th Cir. 2003); *Travelers Indemnity Co. v. United Food & Commercial Workers Int'l Union*, (D.C. 2001); *Stonewall Ins. Co. v. Taylor*, 12 Va.Cir. 372 (Richmond 1988).

When Does Employer Have "Cause" for Termination?

Most employment relationships are "at will," meaning that the employee can quit or be fired at any time, for any reason or for no reason. In other words, an employee does not need good cause to quit, and the employer does not need good cause to fire.

Of course, an employer cannot fire for an illegal reason, such as discrimination or so-called wrongful discharge. See "Wrongful Termination Update," *Employer Alerts!*, Oct. 2001, p. 1; and "Red Cross May Fire Employee for Reporting Blood-Handling Violations," *Employer Alerts!*, July 2002, p. 4. Nor may an employer fire without cause if he has a contract with his employee that only permits termination for cause.

Why would an employer enter into a contract limiting its right to fire? The employer might find itself in a tight labor market and need to offer the security provided by a contract of employment. Or the employer may have unintentionally made promises in its employee handbook that effectively convert the handbook into a contract of employment. See "Employee Handbooks as Employment Contracts," *Employer Alerts!*, Aug. 2002, p. 1. In any event, there are circumstances in which an employer finds itself able to fire only for cause.

What does "cause" or "good cause" mean in this context? The parties to a contractual arrangement are free to define the term in their contract For example, if the employee needs a particular license in order to work (a plumbing license, for example), suspension or revocation of the license might be listed as a cause for termination. Convictions for certain types of crimes, repeated insubordination, drunkenness, and physical assaults on customers or fellow employees might also be on the list. When an employer has decided to offer a contract of employment (or when a highly desirable employee insists on one), the employer should take the time to define "cause" in the contract.

Absent a contractual definition of "cause," there may be various do's and don'ts set out in a employee handbook or job description that serve as a guide. In addition, the employment relationship itself implies certain duties on the part of the employee, including a duty to show up for work in reasonably fit condition, a duty to have and exercise reasonable skill in performing the job, a duty of loyalty and honesty, and a duty to refrain from insubordinate and threatening behavior. A substantial breach of any of these explicit or implied duties is cause for termination.

When the parties themselves have not spelled out what they mean by "cause," courts have defined the term along the following lines –

> fair and honest reasons, regulated by good faith on the part of the employer, that are not trivial, arbitrary or capricious, unrelated to business needs or goals, or pretextual. A reasoned conclusion, in short, supported by substantial evidence gathered through an adequate investi-

gation that includes notice of the claimed misconduct and a chance for the employee to respond.

In a recent Wyoming case, the Court adopted a definition similar to the above. The Court went on to say that, in determining whether an employer had cause for termination, the question isn't, "Did the employee in fact commit the act leading to termination?" Rather, the question is, "Was the factual basis on which the employer concluded a dischargeable act had been committed reached honestly, after an appropriate investigation and for reasons that are not arbitrary or pretextual?" In other words, the courts are not going to second-guess an employer's business judgment so long as the decision to terminate is reached honestly and fairly.

Case reference. *Life Care Centers of America v. Dexter*, 65 P.3d 385 (Wyo. 2003).

Workers' Compensation Update

A number of unusual workers' compensation cases were decided by the local courts his past month. We summarize them below.

Washington Hospital Center (D.C.)

Washington Hospital Center (WHC) hired Paul Thielke in January 1992 to work as a compensation analyst. Under District of Columbia law, employees like Thielke who come in contact with patients or patient areas are required to receive an MMR vaccination against measles, mumps and rubella (German measles) before they start work. Thielke, who was scheduled to begin on February 10, was given his vaccination by WHC personnel on February 3.

On February 5, Thielke suffered a blackout and a variety of other neurological symptoms. Over the next two days he complained of being extremely hot or cold, he suffered fatigue and inability to sleep, and he developed a red rash on the left side of his face. Although he reported to work as scheduled, he then went to see a neurologist for testing.

Over the next year and a half, Thielke experienced a number of seizures, one of which occurred while he was driving home, causing an automobile accident in which he was injured. All told, over the six-year period 1992-1998 Thielke had more than 39 seizure episodes.

Although Thielke had suffered a serious head injury while a teenager, he had been completely symptom-free since that accident. Accordingly, and while there was conflicting expert evidence as to the cause of the seizures, on balance it appeared that the MMR vaccination was responsible. So Thielke filed a claim for workers' compensation benefits.

WHC contested the claim, saying that Thielke wasn't really an employee at the time of the vaccination, since he wasn't scheduled to start for another week. Instead, according to WHC, the injury occurred pre-employment and therefore was not covered by the workers' comp statute.

The D.C. Court of Appeals disagreed. It ruled that an injury arises "out of and in the course of" employment if it would not have happened "but for the fact that conditions and obligations of the employment placed claimant in a position where he was injured." Here, but for employment Thielke had no obligation – nor any inclination so far as the facts showed – to be vaccinated. He did so at WHC's behest to further WHC's interests and for WHC's benefit. That, said the Court, obligated WHC to provide comp benefits to Thielke.

Saadeh (Maryland)

John Saadeh operated a restaurant in Annapolis known as "Jo's Deli." While Saadeh was waiting on a customer named Ravenet, a dispute arose over Ravenet's food order. Ravenet had apparently been drinking and, when Saadeh tried to calm him down, he

became even more angry. With that, Saadeh insisted that Ravenet leave. Ravenet refused and instead punched Saadeh in the face, breaking his nose and inflicting other injuries.

Saadeh underwent surgery for his broken nose, remaining under a doctor's care for several months. But at that point, Saadeh negotiated a settlement of his claims against Ravenet, no doubt thinking his medical problems were over. The settlement provided for payment of $50,000 to Saadeh in exchange for a full release.

Unfortunately, only three months after signing the release, Saadeh suffered a spontaneous dissection of his right carotid artery, which produced serious medical complications. According to Saadeh's treating physicians, this later problem was the result of the earlier attack.

Having released Ravenet from further liability, Saadeh turned to the workers' compensation policy that covered his restaurant. The compensation carrier, Ohio Casualty, contested the claim on the basis of Maryland's workers' comp statute, which says –

> When a person other than an employer is liable for the injury or death of a covered employee for which compensation is payable under this title, the covered employee or, in case of death, the personal representative or dependents of the covered employee may: (1) File a claim for compensation against the employer under this title; or (2) Bring an action for damages against the person liable for the injury or death ...

According to Ohio Casualty, this statute requires employees who are injured by third parties to make an election of remedies – to elect between pursuing a comp claim or suing the third party.

In addition, said Ohio Casualty, by releasing his claims against Ravenet without Ohio Casualty's knowledge or consent, Saadeh effectively extinguished Ohio Casualty's right of subrogation. (Under Maryland's and most other state's laws, when an employer or insurance carrier pays comp benefits, the employer or carrier is "subrogated" to the injured employee's rights against third parties, meaning that they can sue third parties to recover the amount of comp benefits they paid to the injured employee.)

The Maryland Court of Special Appeals (Maryland's intermediate appellate court) agreed with Ohio Casualty and denied comp benefits to Saadeh. It said that Saadeh's initial decision to pursue a claim against Ravenet was not, standing alone, necessarily a final election of remedies, since such an election is only binding if the insurance carrier can show that it was prejudiced. Here, however, Ohio National clearly was prejudiced when Saadeh released Ravenet, thereby barring Ohio National's right to pursue subrogation against Ravenet.

Podgurski (Maryland)

In the Saadeh case, the injured employee pursued a third party who had injured him *before* seeking workers' comp benefits. Somewhat different rules apply when the employee seeks comp benefits first.

Once an injured employee has received comp benefits, Maryland law provides that the employer (or his insurance carrier) has the exclusive right for two months after a compensation award to file suit against a third party who caused the injury. After the two-month period has expired, both the employer and the employee may sue the third party. But regardless of who files the suit, the workers' comp statute grants the employer a lien against any third-party recovery for the full amount of any comp benefits it has paid.

But suppose the injured employee can only recover a portion of his damages from a third party – should he still have to reimburse his employer for the full amount of the comp benefits he received? That was the question in *Podgurski v. One Beacon Ins. Co.* decided by the

Maryland Court of Appeals on April 10.

Deborah Podgurski worked as a hairstylist for Hairstylist Management Systems (HMS) within a Montgomery Ward department store in Frederick, Maryland. While working, she slipped on water leaking from defective plumbing and severely injured her knee. As a result of her injuries, Podgurski received workers' comp benefits of some $11,700. She also sued Montgomery Ward and obtained a judgment of $90,000. Unfortunately, Montgomery Ward was in bankruptcy, and the bankruptcy court allowed her to recover only $26,600 (about 29%) of her judgment.

Although Podgurski recognized that she had to reimburse HMS for the comp benefits it had paid her, she argued that she should not have to reimburse the full $11,700. Her theory was that, as established in her suit against Montgomery Ward, her actual damages were $90,000. Since the bankruptcy court limited her to recovering only 29% of her actual damages, HMS should only be reimbursed at the 29% rate as well.

While Podgurski's argument has a certain ring of fairness, the Court of Appeals wouldn't go along, saying it was bound by the worker's comp statute. Since Podgurski received a third party recovery that exceeded HMS's comp payments to her (even though her actual damages were apparently much higher), the statute required her to reimburse HMS for the full amount of its comp payments.

Mendez (D.C.)

In the Washington metropolitan area, where three jurisdictions are in close proximity, it is possible that several workers' comp statutes might cover a particular injury. When that is the case, the employee usually tries to choose the jurisdiction that pays the higher comp benefits. But that wasn't good enough for Wilberto Mendez. He decided to file two benefit claims.

Mendez, a Virginia resident, was employed by Chamberlin-Washington, Inc., a Maryland corporation, to do work throughout the Washington area. While working in the District, he fell from a scaffold and was injured. He filed for benefits in D.C. and, although the employer disputed his claim on the ground that Mendez's work in D.C. was only "temporary and intermittent" (meaning that the D.C. comp statute would not apply), he was awarded benefits.

The employer later discovered that Mendez had also applied for and received comp benefits in Maryland for the same injury. So it asked the D.C. Department of Employment Services to reopen the case and terminate D.C. benefits. The D.C. Court of Appeals agreed that the receipt of benefits under Maryland law amounted to a change of condition allowing D.C. to reconsider and cancel his comp award.

While the decision is clearly reasonable, one wonders how the employer could have overlooked two separate comp claims for the same injury in the first place.

Case references. *Washington Hosp. Center v. D.C. Dept. of Employment Services*, 2003 WL 1922817 (D.C. 2003); *Saadeh v. Saadeh, Inc.*, 2003 WL 1610809 (Md.App. 2003); *Podgurski v. One Beacon Ins. Co.*, 2003 WL 1860857 (Md. 2003); *Mendez v. D.C. Dept. of Employment Services* 2003 WL 1562073 (D.C. 2003).

Congress, DOL Propose Major Wage and Hour Law Changes

The Fair Labor Standards Act, together with regulations of the Department of Labor, constitute a complicated, rigid, and at times archaic set of wage and hour rules. Recent proposals, if adopted, will go a long way to changing that.

Family Time and Workplace Flexibility Act

The FLSA has long prohibited comp time in exchange for overtime worked by non-exempt employees, except in very limited circumstances. This measure would give some much needed flexibility to existing rules.

Under the bill, an employee may enter into a voluntary agreement with his employer to receive compensatory time at the rate of 1½ hours for each hour of overtime worked. The agreement must be entered into *before* performance of the overtime that is the subject of the agreement, and the employee cannot accumulate more than 160 hours of comp time. Any comp time not used during a given year must be cashed out at the usual, time-and-a-half overtime rate by January 31 of the following year. The employee may cancel the agreement at any time on 30 days' notice; upon cancellation, the employer must cash out any accrued but unused comp time.

The proposal would also allow employers to establish an 80-hour biweekly work schedule without having to pay overtime, provided no more than 50 hours are worked in any one week. In other words, up to 10 hours of overtime in one week may be traded for a like amount of comp time in the other week. Under current law, work in excess of 40 hours per week triggers an overtime obligation, even if the employer has a biweekly work schedule.

Finally, an employer may establish a "flexible credit hour program" which permits an employee, by prior arrangement with the employer, to accrue up to 50 flexible credit hours.

Participation in any of these three new programs would be limited to employees who have worked 1,250 hours during the previous 12 months. In non-union shops, participation would be entirely voluntary on the employee's part. In union shops, the bargained-for terms of the collective bargaining agreement would govern.

"White Collar" Exemptions to Minimum Wage and Overtime Requirements

The FLSA exempts executives, administrators, professionals and outside sales employees from the Act's minimum wage and overtime requirements. Although the Act itself does not define those terms, it does give the Department of Labor authority to do so. The basic definitions, which include both minimum salary requirements and job descriptions, have remained essentially unchanged for years.

DOL's proposed new regs would eliminate the so-called "long test" and "short test" for executives, administrators and professionals and substitute a "standard test." The salary component of each test would be raised to $425 per week. (Neither the current test nor the new proposal contains a salary test for outside sales employees.) The job descriptions would also be clarified and simplified.

The new regs would contain a special exemption for highly compensated employees – employees who earn more than $65,000 per year in base salary, commissions and non-discretionary bonuses – so long as they have an identifiable executive, administrative or professional function.

Under current rules, an executive, administrator or professional must be "salaried" to qualify as exempt. See "Exempt Employees and the 'Salary Basis' Requirement," *Employer Alerts!*, April 2001, p. 1. An employee will generally not be considered salaried if the employer docks his pay for disciplinary reasons. The proposed regulations would retain that requirement, but would allow employers to suspend exempt employees without pay for discriminatory harassment.

The proposed rules would also clarify the "window of correction" concept, under which an employer who has taken improper deductions from the pay of an exempt employee may refund those deductions to retain the employee's exempt status. See "FLSA's 'Window

of Correction,'" *Employer Alerts!*, March 2003, p. 3. In addition, the rules would create a safe harbor provision: if an employer has a written policy prohibiting improper pay deductions, he notifies employees of the policy, and he reimburses employees for any improper deductions, then the employees involved will not lose their exempt status on account of the improper deductions unless the policy is repeatedly and willfully violated.

Statutory reference. S. 317 (Family Time and Workplace Flexibility Act), 108th Cong., 1st Sess.

Regulatory reference. 29 C.F.R. Part 541 (proposed), 68 Fed.Reg. 15560 (March 31, 2003).

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