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8th Biennial

EMPLOYMENT
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June 2002



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8TH BIENNIAL

EMPLOYMENT LAW INSTITUTE

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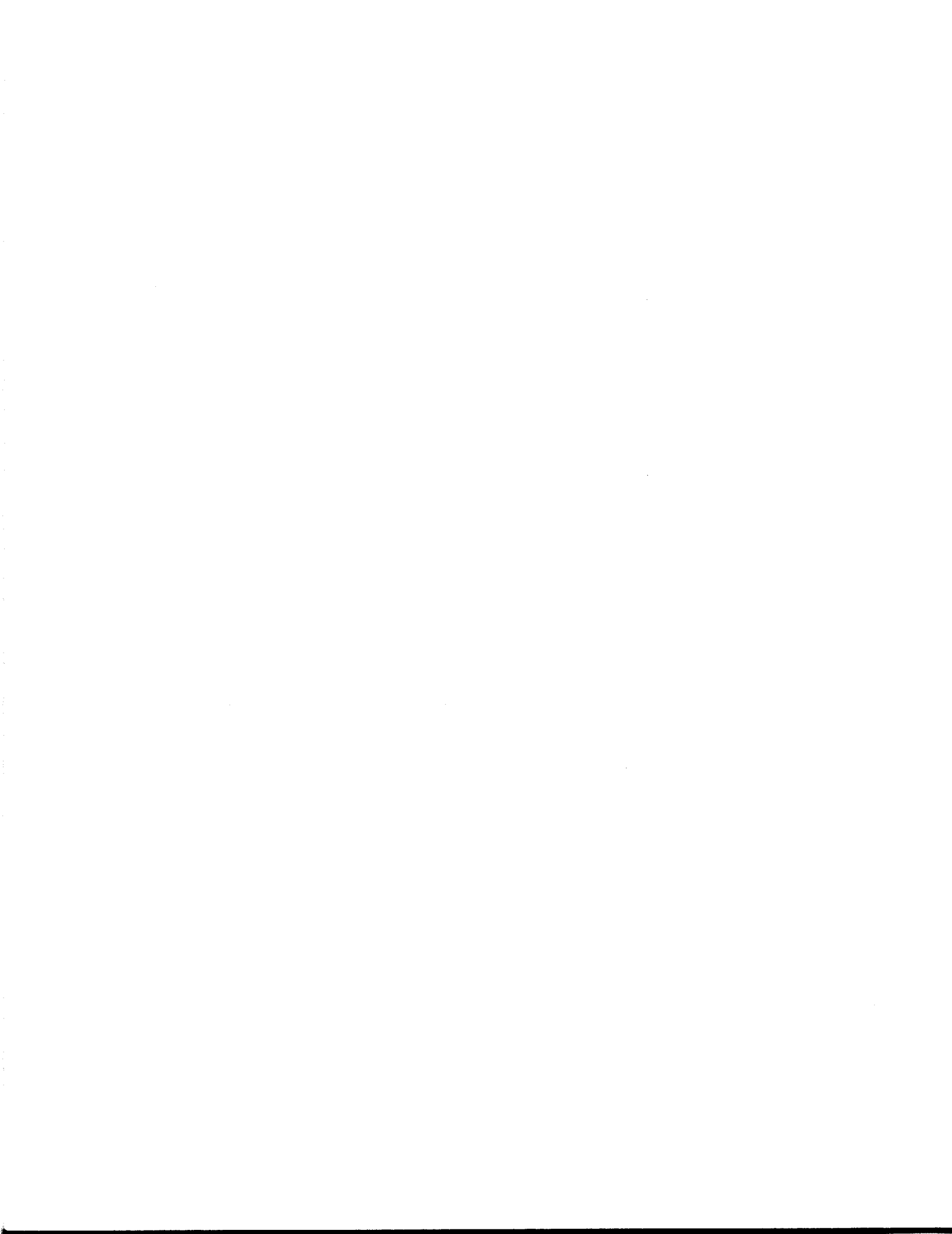
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**EMPLOYMENT DISCRIMINATION UPDATE
2000-2002**

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SECTION A



**EMPLOYMENT DISCRIMINATION UPDATE
2000-2002**

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Update on the Law of Discrimination

I. Introduction

- Arbitration Decisions

See materials on "Arbitration Provisions: The Aftermath of Circuit City Stores, Inc. v. Adams and EEOC v. Waffle House" prepared for the 8th Biennial Employment Law Institute by Hon. Robert D. Hudson, Greenebaum Doll & McDonald, Covington, Kentucky.

- Harassment Decisions

See materials on "Workplace Harassment: A Critical Update" prepared for the 8th Biennial Employment Law Institute by Hon Winifred L. Bryant, Greenebaum, Doll, & McDonald, Lexington, Kentucky and Hon. Julie K. Hackworth, Ashland, Inc., Covington, Kentucky.

- Disability Discrimination Decisions [ADA]

See materials on "The Americans with Disabilities Act; An Analysis of Recent Decisions" prepared for the 8th Biennial Employment Law Institute by Hon. Raymond C. Haley, III and Hon. Kathryn A. Quackenbush, Woodward, Hobson & Fulton, Louisville, Kentucky.

- Religious Discrimination Decisions

See materials on "Losing My Religion: The Employer's Duty to Accommodate an Employee's Religious Beliefs" prepared for the 8th Biennial Employment Law Institute by Hon. Debra H. Dawahare, Wyatt, Tarrant & Combs, Lexington, Kentucky.

II. U.S. Supreme Court and Sixth Circuit Decisions

A. Disparate Treatment Discrimination – Establishing the Prima Facie Case

1. Background

a. McDonnell Douglas Corp. v. Green, 411 U.S. 792 (1973), established the basic evidentiary framework for Title VII (42 U.S.C. §2000e *et seq.*) disparate treatment claim. See also, Texas Dept. of Community Affairs v. Burdine, 450 U.S. 248 (1981). The plaintiff must show:

- i. membership in a protected group;
- ii. qualified for the position;
- iii. rejection or other adverse employment action; and

- iv. circumstances supporting an inference of discrimination.¹

Burden of going forward then shifts to the employer to articulate a legitimate, nondiscriminatory reason for the adverse action;² and

Then the burden is on plaintiff to prove that the reason articulated by the employer was a pretext for discrimination. That is, the plaintiff must meet the ultimate burden of persuading the court that the plaintiff was the victim of intentional discrimination.

This burden can be met either by directly persuading the Court that a discriminatory reason more likely motivated the employer or indirectly by showing that the employer's proffered explanation is unworthy of credence. Texas Department of Community Affairs v. Burdine, 450 U.S. 248, 256 (1981).

- b. St. Mary's Honor Center v. Hicks, 509 U.S. 502 (1993) held that rejection by the fact finder of the employer's asserted reason does not entitle the plaintiff to a judgment as a matter of law. It still remains for the factfinder to determine whether the plaintiff's proffered reason (intentional discrimination) is correct. The factfinder's disbelief of the reason put forward by the employer (particularly if disbelief is accompanied by a suspicion of mendacity) may, together with the elements of the prima facie case be enough to show intentional discrimination.
2. Reeves v. Sanderson Plumbing Products Inc., 530 U.S. 133 (2000).³ The Court:
- a. Rejected the "pretext plus" theory that some courts thought was required by St. Mary's Honor Center decision;

¹ In Clayton v. Meijer, Incorporated, 281 F.3d 605 (6th Cir. 2002) the Court held that an employee can satisfy this element of the McDonnell Douglas test by proving that the employee was replaced by a person not within the protected class or by showing that similarly situated, non-protected employees were treated more favorably. See also, Hoskins v. Oakland County Sheriff's Department, 227 F.3d 719 (6th Cir. 2000)(as female former deputy sheriff was not similarly situated to male deputies who were accommodated by county, she failed to establish a prima facie Title VII case).

² In Smith v. Leggett Wire Company, 220 F.3d 752 (6th Cir. 2000) the Court held that an employee's threat to "kill a bunch" of people unless his pay dispute was resolved constituted a legitimate nondiscriminatory reason for termination.

³ In accord, Braithwaite v Timken Company, 258 F.3d 488 (6th Cir. 2001).

- b. Made it clear that a plaintiff can prevail merely by making out a prima facie case and presenting enough evidence that the employer's reason was pretextual without additional, independent evidence of discrimination; and
 - c. Reasoned that "in appropriate circumstances, the trier of fact can reasonably infer from the falsity of the explanation that the employer is dissembling to cover up a discriminatory purpose."
3. Swierkiewicz v. Sorema N. A., 534 U.S. 506 (2002).
- a. The McDonnell Douglas framework is an evidentiary standard, not a pleading requirement. The framework does not apply where a plaintiff is able to produce direct evidence of discrimination. See Trans World Airlines, Inc. v. Thurston, 469 U.S. 111 (1985). Because, the precise requirements of a prima facie case can vary depending on the context, the framework was "never intended to be rigid, mechanized, or ritualistic." Furnco Constr. Corp. v. Waters, 438 U.S. 567 (1978).
 - b. A Title VII or Age Discrimination in Employment Act (29 U.S.C. §623 [ADEA]) complaint alleging disparate treatment discrimination is sufficient to survive a motion to dismiss if it satisfies Federal Rule of Civil Procedure 8(a)(2) that a complaint must include only "a short and plain statement of the claim showing that the pleader is entitled to relief." The statement must merely give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests. Thus, complaints in employment discrimination cases must satisfy only the requirements of Rule 8(a).
 - c. **NB:** Abrogates the 6th Circuit's decision Jackson v. Columbus, 194 F.3d 737 (1999) which held that the complaint must contain factual allegations that support each element of the McDonnell Douglas prima facie case.
- B. Disparate Impact Discrimination – Establishing a Prima Facie Case
1. Background
 - a. Under Title VII, impermissible disparate impact discrimination arises from employment practices that are "fair in form but discriminatory in operation." Griggs v. Duke Power Co., 401 U.S. 424 (1971). Disparate impact does not require a showing of discriminatory intent.

- b. As a general rule, the plaintiff must identify a particular employment practice and offer statistical evidence demonstrating that the employment practice has a significant adverse effect on a protected group. Watson v. Fort Worth Bank & Trust, 487 U.S. 977 (1988).
 - c. Once the plaintiff establishes the adverse effect, the burden shifts to the employer to produce evidence that the challenged practice is a business necessity.
2. Adams v. Florida Power Corp., ___ U.S. ___, 122 S.Ct. 1290 (2002); 255 F.3d 1322(11th Cir. 2001).
- a. The Court granted *cert* to resolve a Circuit split whether the disparate impact theory of discrimination is available to plaintiffs under the ADEA.
 - b. In Hazen Paper Co. v. Biggens, 507 U.S. 604 (1993), a case involving liquidated damages under the ADEA, the Court expressly left open the question of "whether a disparate impact theory of liability is available under the ADEA."
 - c. The Second, Eighth and Ninth Circuits subsequently held that disparate impact claims are actionable under the ADEA. See Criley v. Delta Air Lines, Inc., 119 F.3d 102 (2d Cir. 1997); Lewis v. Aerospace Cmty. Credit Union, 114 F.3d 696 (8th Cir. 1997); and Frankv. United Airlines, Inc., 216 F.3d 845 (9th Cir. 2000).
 - d. In contrast, the First, Third, Sixth, Seventh and Tenth Circuits have questioned the viability of disparate impact claims under the ADEA post-Hazen. See Mullin v. Raytheon Co., 164 F.3d 696 (1st Cir.) *cert. denied*, 528 U.S. 811 (1999); EEOC v. Francis W. Parker School, 41 F.3d 1073 (7th Cir. 1994); Ellis v. United Airlines, Inc., 73 F.3d 999 (10th Cir. 1996); DiBiase v. SmithKline Beecham Corp., 48 F.3d 719 (3d Cir. 1995); and Lyon v. Ohio Educ. Ass'n and Prof'l Staff Union, 53 F3d 135 (6th Cir. 1995).
 - e. Writ of certiorari was dismissed as improvidently granted.
3. Alexander v. Sandoval, 532 U.S. 275 (2001).
- a. §601 of Title VI of the Civil Rights Act of 1964 prohibits discrimination based on race, color, or national origin in covered programs and activities. 42 USC §2000d.

- b. Pursuant to §602 of Title VI (42 USC §2000d-1) which authorizes federal agencies to effectuate §601 by issuing regulations, the Department of Justice promulgated a regulation forbidding funding recipients from using criteria or administrative methods that had the “effect” of subjecting individuals to discrimination based on the prohibited grounds (disparate impact).
- c. Reaffirmed that there is a private right of action to enforce the text of §601 (See Cannon v. University of Chicago, 441 U.S. 677 (1979)) which prohibits intentional discrimination.
- d. However, the Court held that there is no private right of action to enforce the DOJ’s disparate impact regulation it promulgated pursuant to §602.

C. Damages

1. Caps

- a. 42 U.S.C. §1981(a) provides that: “The sum of the amount of compensatory damages awarded . . . for future pecuniary losses, emotional pain, suffering, inconvenience, mental anguish, loss of enjoyment of life, and other nonpecuniary losses, and the amount of punitive damages awarded . . . shall not exceed. . .” various amounts based on the number of employees the employer has.
- b. Pollard v. E.I. du Pont de Nemours & Co., 532 U.S. 843 (2001).
 - i. The Court held that an award of front pay to compensate a successful plaintiff for lost pay between the time of judgment and reinstatement was not subject to the damage caps in 1991 Civil Rights Act for “compensatory damages.”
 - ii. **NB:** Abrogates the 6th Circuit’s decision in Hudson v. Reno, 130 F.3d 1193 (6th Cir. 1997), which held that the statutory damage caps under §1981 applied to all compensatory and punitive damages in the entire lawsuit including front pay.

2. Punitive Damages

a. Definition

42 U.S.C. §1981a(b)(1) provides that: “A complaining party may recover punitive damages under this section against a respondent (other than a government,

government agency or political subdivision) if the complaining party demonstrates that the respondent engaged in a discriminatory practice or discriminatory practices with malice or with reckless indifference to the federally protected rights of an aggrieved individual.”

b. Cooper Industries, Inc. v. Leatherman Tool Group, Inc., 532 U.S. 424 (2001).

i. This was an unfair competition and false advertising case under the Lanham Act⁴, not a Title VII case.

ii. The due process clause of the U.S. Constitution prohibits the award of *excessive* punitive damages. See BMW of North America, Inc. v. Gore, 517 U.S. 559 (1996),

iii. When a Court of Appeals reviews a District Court determination of the constitutionality of a punitive damage award, it should apply a *de novo* standard and not the less demanding abuse-of-discretion standard.

3. Back Pay Awards – Taxes

a. United States v. Cleveland Indians Baseball Co., 532 U.S. 200 (2001).

This was not a Title VII case. However, the Court found that payroll taxes imposed on back wages should be computed using the rate and wage base applicable in the year in which the back wages were actually paid, not the year in which they should have been paid.

b. **NB:** Abrogates the 6th Circuit's decision in Bowman v. United States, 824 F.2d 528 (1987) that held that back wages were subject to taxation in the years to which back pay related.

D. Sovereign Immunity

1. Background

a. U.S. Const. Amend. 11 provides that:

“The Judicial power of the United States shall not be construed to extend to any suit in law or equity,

⁴ The Lanham Act is the popular name for the Trademark Act of 1946.

commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State.”

- b. Since 1996, the Supreme Court has held that the 11th Amendment shields unconsenting states from private lawsuits seeking damages for alleged violations of the Age Discrimination in Employment Act (Kimel v. Florida, 528 U.S. 62 (2000)); the False Claims Act (Vermont Agency of Natural Resources v. U.S. ex rel. Stevens, 529 U.S. 765 (2000)); the Lanham Act (College Savings Bank v. Florida Prepaid Postsecondary Ed. Expense Brd., 527 U.S. 666 (1999)), the Patent Act (Florida Prepaid Postsecondary Educ. Expense Bd. V. College Sav. Bank, 527 U.S. 627 (1999)), the Fair Labor Standards Act (Alden v. Maine, 527 U.S. 706 (1999)) and the Indian Gaming Regulatory Act (Seminole Tribe of Fla. V. Florida, 517 U.S. 44 (1996)).
- c. There is no Eleventh Amendment bar to private lawsuits seeking damage remedies against a state in three instances:
 - i. when the state has consented to suit;
 - ii. when Ex Parte Young exception applies;⁵ or
 - iii. when Congress has properly abrogated states’ immunity.
- d. Congress can abrogate Eleventh Amendment immunity under its Section 5 power to enforce the 14th Amendment if (Seminole Tribe of Florida v. Florida, 517 U.S. 44 (1996)):
 - i. Congress unequivocally expressed its intent to abrogate the immunity; and
 - ii. Congress acted pursuant to a valid exercise of its Section 5 power as determined by the requirement that there be:
 - 1) congruence; and
 - 2) proportionality between the injury to be prevented or remedied and the means

⁵ A plaintiff may sue a *named state officials* in their “individual and official capacity” for alleged violations of federal laws or the Constitution if they are seeking prospective relief such as an injunction to prevent a continuing violation of federal law, but not for relief designed to remedy past behavior such as damages.

adopted to that end. City of Boerne v. Flores, 521 U.S. 507 (1997).

2. Board of Trustees of the University of Alabama v. Garrett, 531 U.S. 356 (2001).
 - a. Adds the Americans with Disabilities Act (ADA) to the list of federal statutes that can't be enforced against the states by private lawsuits seeking damages.
 - b. To abrogate the states' 11th Amendment immunity from suit by an individual in federal court, two factors must be met:
 - i. Congress must make its intention to do so unmistakably clear; and
 - ii. The congressional enactment must be a proper exercise of Congress' constitutional authority.
 - c. ADA was an invalid exercise of Congress' 14th Amendment, Section 5 power against the states because Congress failed to establish a pattern of irrational state discrimination in employment against the disabled. Moreover, the rights and remedies created by the law were not "congruent and proportional" to targeted violations.
3. Raygor v. Regents of the University of Minnesota, 534 U.S. 533 (2002).
 - a. State university employees brought an action in federal district court alleging a federal cause of action under the ADEA against their employer and coupled it with a state age discrimination action pursuant to 28 U.S.C. §1367, a federal supplemental jurisdiction statute. The federal statute purports to toll the statute of limitations period for state supplemental claims while the state and federal claims are pending in federal court and for 30 days after they are dismissed.
 - b. The plaintiffs' ADEA claims were dismissed because they were barred by the 11th Amendment. Thereafter, Plaintiffs refiled their state law claims in state court beyond the state statute of limitations for such claims, but within the 30 day tolling period under 28 U.S.C. §1387.
 - c. The Court held that the state law claims should have been dismissed as time-barred because, as a matter of statutory construction, the tolling provision does not apply to state

law claims asserted against nonconsenting states that are subsequently dismissed on 11th Amendment grounds.

- d. Expressly refused to address whether federal tolling of a state statute of limitations constitutes an abrogation of state sovereign immunity with respect to claims against state defendants. "[W]e can say that the notion at least raises a serious constitutional doubt."
 - e. See, Jinks v. Richland County, S.C., 2002 W.L. 654174 (4/2/02). The South Carolina Supreme Court answered the question left open in 2002 W.L. 654174 (4/2/02). The South Carolina Supreme Court answered the question left open by the U.S. Supreme Court in Raygor. It held that the tolling provision in §1367(d) violates the Tenth Amendment⁶ because it interferes with the state's sovereign power to set conditions for the waiver of its subdivisions' immunity from tort actions.
4. Johnson v. University of Cincinnati, 215 F.3d 561 (6th Cir. 2000).
- a. A terminated vice president sued the university under Title VII for race and national origin discrimination and retaliatory discrimination.
 - b. Relying on the Supreme Court's decision in Fitzpatrick v. Bitzer, 427 U.S. 445, 456, 96 S.Ct. 2666, 49 L.Ed.2d 614 (1976) that Congress had abrogated the states' sovereign immunity by enacting Title VII under § 5 of the Fourteenth Amendment, the 6th Circuit found that the 11th Amendment conferred no immunity upon the university from the Title VII claims.
5. Kovacevich v. Kent State University, 224 F.3d 806 (6th Cir. 2000).
- a. A faculty member sued the university for sex and age discrimination under the Equal Pay Act (29 U.S.C. §206(d) [EPA]); Title VII and the ADEA.
 - b. On appeal from a judgment in favor of the plaintiff, the university raised, for the first time, an Eleventh Amendment defense.
 - c. In Wisconsin Dep't of Corrections v. Schacht, 524 U.S. 381 (1998) the U.S. Supreme Court stated that the Eleventh

⁶ The Tenth Amendment provides "the powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively or to the people." U.S.Const. amend. X. "

Amendment is not jurisdictional, and is not akin to the complete diversity requirement. A court is not required to raise the defect on its own. Unless the state raises the matter, a court can ignore it.⁷

- d. Nonetheless, the Sixth Circuit held that the Eleventh Amendment defense “sufficiently partakes of the nature of a jurisdictional bar that it may be raised at any point of the proceedings,” including appeal.
 - e. Because the university was an “arm of the state” it was entitled to Eleventh Amendment immunity on the ADEA claim. See Kimel v. Florida Bd. of Regents, 528 U.S. 62 (2000).
 - f. However, the Court found that the Equal Pay Act constituted a proper abrogation by Congress of the states’ Eleventh Amendment immunity. It reaffirmed the continuing validity of Timmer v. Michigan Dep’t of Commerce, 104 F.3d 8333 (6th Cir. 1997).
6. An Aside: Fisher v. Peters, 249 F.3d 433 (6th Cir. 2001).
- a. An employee with the dual status as both a civilian and National Guard technician brought a Title VII suit against the acting secretary of the U.S. Air Force claiming sex discrimination, retaliation, and sexual harassment.
 - b. Relying on Chappell v. Wallace, 462 U.S. 296 (1983)(Congress has exercised its plenary authority over the military by establishing statutes regulating military life and providing for a comprehensive internal system of justice), the Sixth Circuit reiterated its refusal to extend to uniform members of the armed forces the statutory remedies (e.g., Title VII) available to civilians absent a clear direction from Congress to do so. See Coffman v. States of Michigan, 120 F.3d 57 (6th Cir. 1997).
 - b. The Court held that National Guard technicians occupy military positions despite their hybrid employment status. Therefore, they had no remedy under Title VII.⁸

⁷ This decision abrogated the Sixth Circuit’s decision in Wilson-Jones v. Caviness, 99 F.3d 203 (1996) that held “state immunity is jurisdictional in the same sense as the complete diversity requirement” and that “neither the litigants’ consent, nor oversight, nor convenience can justify a court’s exercise of illegal power.”

⁸ See, also Kentucky Department of Military Affairs v. Hon. Robert L. Crittenden, 2001 WL 958909 (KyApp Aug. 24, 2001). Discrimination and retaliation claims brought under KCRA for discrimination and retaliation by current and former members of the Kentucky National Guard

E. Attorney's Fees and Procedural Issues

1. Attorney's Fees

a. Buckhannon Board & Care Home Inc. v. West Virginia Dep't. of Health and Human Resources, 532 U.S. 598 (2001)

- i. Involved only the fee-shifting provisions in the 1988 Fair Housing Amendments Act and the 1990 ADA, but the Court noted that the same language appears in other statutes, including the 1964 Civil Rights Act and 42 U.S.C. §1988, authorizing the award of attorney's fees to the "prevailing party".
- ii. Court held that a "prevailing party" entitled to an award of attorney's fees is one who has been awarded some relief by the court.
- iii. An enforceable judgment on the merits and court-ordered consent decrees create the "material alteration of the legal relationship of the parties" sufficient to permit an award of attorney's fees.
- iv. Rejected the "catalyst theory" which would have permitted the award of attorney's fees when the plaintiff's lawsuit brings about the desired change in the defendant's conduct without a final judgment or court-ordered consent decree.

b. Adcock-Ladd v. Secretary of Treasury, 227 F.3d 343 (6th Cir. 2000).

- i. 42 U.S.C. §§ 2000e-5(k) & 2000e-16(d) authorize, in employment discrimination lawsuits, the discretionary court-awarded allowance of a reasonable attorney fee, as a recoverable litigation-cost, in favor of the prevailing parties, other than the United States.
- ii. Plaintiff, a former Secret Service agent, filed her employment discrimination lawsuit in Tennessee. She retained a Washington, D.C. lawyer to depose a key witness in that city. The Plaintiff ultimately prevailed.

against the Kentucky Department of Military Affairs and Kentucky National Guard were impliedly preempted by federal law.

- iii. The Sixth Circuit found that the District Court abused its discretion because it applied the reasonable hourly rate that prevailed in Knoxville, the situs of the court of record, to out-of-town counsel's services rather than the proven reasonable hourly charge the out-of-town attorney billed for legal work performed in Washington, D.C..
- iv. The Sixth Circuit distinguished its decision in Hudson v. Reno, 133 F.3d 1193 (6th Cir. 1997), cert. Denied, 525 U.S. 822 (1998) which deemed the legal community within the court's territorial jurisdiction as the relevant community for determining the reasonable hourly rate. It held that Hudson governs fee awards to out-of-town counsel who volitionally elect to represent a party in a lawsuit to be litigated in the jurisdiction of a court in which the case is filed instead of using the judicial venue of the lawyer's professional residence. In the Adcock-Ladd case, the Plaintiff retained out-of-town counsel because she was required to depose a witness in Washington, D.C. and out-of-town counsel transacted all his professional duties for the plaintiff within the District of Columbia.

2. Statute of Limitations

- a. Edelman v. Lynchburg College, ___ U.S. ___, 122 S.Ct. 1145 (2002).
 - i. Title VII §706(e)(1) requires that an employee alleging employment discrimination to file a "charge" with the EEOC within a certain time after the conduct alleged (USC §2000e-5(e)(1) and §706(b) requires the employee to affirm or swear that the allegations are true (USC §2000e- 5(b)).
 - ii. The Court found that a letter faxed by an employee to an EEOC field office within the required statutory time period claiming "gender-based employment discrimination, exacerbated by discrimination on the basis of . . . national origin and religion" constituted a "charge" within the meaning of §706(e)(1) even though neither the complainant nor the EEOC had treated it as one.
 - iii. The Court sustained the validity of an EEOC regulation that permits an otherwise timely filer to

verify a charge after the time for filing has expired.
See 29 CFR §11601.12(b)(1997).

- b. Burzynski v. Cohen, 264 F.3d 611 (6th Cir. 2001).
 - i. ADEA contains no statute of limitations for a federal employee who pursues administrative remedies before going to court.⁹
 - ii. The Court held that Title VII's 90-day limitations period for filing a civil action applies to ADEA claims brought by federal employees who pursued administrative remedies before going to court. In accord, Rawlette v. Runyon, 104 F.3d 359 (4th Cir. 1996)(unpublished decision); Edwards v. Shalala, 64 F.3d 601 (11th Cir. 1995); and Lavery v. Marsh, 918 F.2d 1022 (1st Cir. 1990). Contra, Lubniewski v. Lehman, 891 F. 2d 216 (9th Cir. 1989)(six year statute of limitations under 28 U.S.C. §2401(a) applies).
- c. Amini v. Oberlin College, 259 F.3d 493 (6th Cir. 2001).
 - i. Plaintiff's application for a tenure-track faculty position was rejected. He did not file his race, religion, national origin and age discrimination charges with the EEOC until more than 300 days¹⁰ elapsed after receipt of the college's written notification that he was not going to be hired. However, his charges were filed within 300 days of when he learned that the college hired a white male under the age of 40 for the position who did not subscribe to the same religious beliefs as the plaintiff.
 - ii. The court held that the starting date for the 300-day limitations period is when the plaintiff learns of the employment decision itself, not when the plaintiff learns that the employment decision may have been discriminatorily motivated. See also, EEOC v. United Parcel Service, 249 F.3d 557 (6th Cir. 2001).

⁹ Federal employees alleging age discrimination do not have to seek relief from their employing agency or the EEOC. They can opt to file suit in federal court in the first instance. However, they can elect to pursue administrative remedies first. 29 U.S.C. §633a(d).

¹⁰ Because the alleged unlawful practice occurred in a "deferral state," the plaintiff had 300, instead of 180, days in which to file a discrimination charge with the EEOC. 42 U.S.C. §2000e-5(e).

- iii. The Supreme Court has held that the 300-day period of limitations for filing a charge with the EEOC is subject to waiver, estoppel, and equitable tolling (Zipes v. Trans World Airlines, 455 U.S. 385 (1982).
- iv. However, the Sixth Circuit held that equitable tolling of the EEOC filing period in this case did not satisfy its five-factor test (Truitt v. County of Wayne, 148 F.3d 644 (6th Cir. 1998):
 - 1) lack of notice of the filing requirement;
 - 2) lack of constructive of constructive knowledge of the filing requirement;
 - 3) diligence in pursuing one's rights;
 - 4) absence of prejudice to the defendant; and
 - 5) the plaintiff's reasonableness in remaining ignorant of the particular legal requirement for filing his claim.
- d. Wade v. Knoxville Utilities Board, 259 F.3d 452 (6th Cir. 2001).
 - i. Employee sued for race discrimination and retaliation under Title VII and the Tennessee Human Rights Act (THRA).
 - ii. Plaintiff argued that the time for filing suit after receipt of the EEOC right-to-sue letter should be tolled because of his lack of mental competency pursuant to TN Code §28-1-106 which provides that: "If the person entitled to commence an action is, at the time the cause of action accrued . . . of unsound mind, such person . . . may commence the action, after the removal of such disability, within the time of limitation for the particular cause of action, unless it exceeds three (3) years, and in that case within three (3) years from the removal of such disability."
 - iii. Consistent with its previous decision in Johnson v. Ry. Express Agency, Inc., 489 F.2d 525 6th Cir. 1973), the Court of Appeals held that state law tolling or savings provisions do not apply to the limitations periods expressly set forth in Title VII.

- e. Cox v. City of Memphis, 230 F.3d 199 (6th Cir. 2000).
- i. White police lieutenants alleged that the city engaged in racially discriminatory failure to promote because of the use of an allegedly tainted eligibility list. The plaintiffs were on the eligibility list despite their allegations that management had coached black police lieutenants for the test that determined inclusion and ranking on the list. The plaintiffs did not file a charge with the EEOC within 300 days of the promulgation of the eligibility roster. However, they did file their charges within 300 days after the eligibility list expired two years later and they had not been selected for promotion.
 - ii. The Court rejected the plaintiffs' claim that the use of the tainted eligibility list constituted "continuing acts" of discrimination thereby excepting them from the usual timing rules for filing a charge of discrimination with the EEOC.
 - iii. The Court held that the promulgation of the tainted promotion roster triggers the time for filing an EEOC charge. Subsequent promotions or hiring decisions based on such a list are not continuing acts, but are merely the effect of previous discrimination. In accord, Bronze Shields, Inc. v. New Jersey Dept. of Civil Service, 667 F.2d 1074 (3d Cir. 1981). Contra, Guardians Ass'n of New York City Police Dept. v. Civil Service Comm'n of City of New York, 633 F.2d 232 (2d Cir. 1980).

3. Standing

- a. Cleveland Branch, National Association for the Advancement of Colored People v. City of Parma, Ohio, 263 F.3d 513 (6th Cir. 2001). The NAACP, an advocacy association, sued the city alleging race discrimination in the recruitment, selection, and hiring of municipal employees.
- b. The Court held that an association may obtain standing to bring suit on behalf of its members when its members would otherwise have standing to sue in their own right, the interests at stake are germane to the organizations' purpose, and neither the claim asserted nor the relief requested requires the participation of individual members in the lawsuit. Citing Friends of the Earth, Inc. v. Laidlaw Envtl. Servs., 528 U.S. 167 (2000).

- c. Court also held that "associational standing" is determined at the time the complaint is filed.

4. Scope of EEOC Investigation

- a. EEOC v. Roadway Express, 261 F.3d 634 (6th Cir. 2001).

- i. 42 U.S.C. §2000e-8(a) provides that:

"In connection with any investigation of a charge filed under section 2000e-5 of this title, the Commission or its designated representative shall at all reasonable times have access to, for the purposes of examination, and the right to copy any evidence of any person being investigated or proceeded against that relates to unlawful employment practices covered by this subchapter and is relevant to the charge under investigation."

- ii. The employer, charged with failure to hire women as operators/laborers and failure to promote blacks to sales/management positions, refused to provide information regarding the promotion of women to sales/management positions and the hiring of blacks as operators/ laborers as not relevant to the charge.

The Court held that the statutory relevancy requirement should be generously construed and that evidence of employer discrimination in one situation or employment position is relevant to a determination of whether the employer discriminated in other circumstances. See Blue Bell Boots, Inc. v. EEOC, 418 F.2d 355 (6th Cir. 1969).

- iii. The employer also refused to turn over evidence that did not fall within the time-frame of the EEOC charge (e.g., post-charge information).

The Court held that the temporal scope of an EEOC request for information was not so limited. Compare, EEOC v. Shell Oil, 466 U.S. 54 (1984).

III. Kentucky Cases

A. Sovereign Immunity

1. Background

- a. Ky.Const. §231 provides: "The General Assembly may, by law, direct in what manner and in what courts suits may be brought against the Commonwealth."
 - b. School districts, as agencies of state government, are entitled to sovereign immunity. Clevinger v. Board of Education, 789 S.W.2d 5 (Ky. 1990).
 - c. While the defense of sovereign immunity usually arises from tort claims, it applies as well to contract claims. University of Louisville v. Martin, 574 S.W.2d 676 (Ky.App. 1978).
2. Ammerman v. Board of Education of Nicholas County, 30 S.W.3d 793 (Ky. 2000).
- a. Teachers sued their school board alleging breach of contract, various tort claims, violation of certain statutes protecting teachers and sexual harassment in violation of Kentucky Civil rights Act. KRS §344.010 *et seq.*
 - b. The Kentucky Supreme Court held that all of the plaintiffs' claims except the one based upon the Kentucky Civil Rights Act were barred by the doctrine of sovereign immunity.
 - c. Reaffirmed the continuing viability of its decision in Department of Corrections v. Furr, 23 S.W.3d 615 (Ky. 2000) that the doctrine of sovereign immunity does not prevent suits based on the Kentucky Civil Rights Act against the Commonwealth or its agencies because the state had specifically waived it.
3. Tiller v. University of Kentucky, 55 S.W.3d 846 (Ky.App. 2001).
- a. Community college employee sued the university for sex discrimination in compensation.
 - b. The university argued that the plaintiff's claims were, in essence, wage discrimination claims under KRS Chapter 337 which contains no waiver of sovereign immunity for wage discrimination claims brought against the Commonwealth.
 - c. While agreeing that sovereign immunity would bar a wage claim based on KRS Chapter 337, the Court concluded that the plaintiff brought her claims under the Kentucky Civil Rights Act, for which sovereign immunity is expressly waived.

B. Procedural and Miscellaneous Matters

1. Definition of Sex Discrimination

- a. KRS §344.040(1) provides in pertinent part that it is an unlawful employment practice for an employer: “otherwise to discriminate against an individual with respect to compensation, terms, conditions, or privileges of employment, because of the individual’s sex.”
- b. KRS §344.030(8) defines the term, “discrimination on the basis of sex” to include pregnancy, childbirth, and other related conditions.
- c. In Tiller v. University of Kentucky, 55 SW3d 846 (Ky.App. 2001) the Court held that discrimination against a female employee on the basis of her status as an unwed mother was sufficiently within the statutory definition of “discrimination on the basis of sex” to allow her to bring a sex discrimination suit against her college assuming the requisite burden of proof is met.

2. Definition of “Employee”

- a. KRS §344.030(5) defines “employee” for purposes of Kentucky Civil Rights Act as “an individual employed by an employer”
- b. In Steward v. University of Louisville, 65 S.W.3d 536 (Ky.App. 2002) the Court held that a graduate student receiving a fellowship from the university that provided full tuition remission and a renewable taxable yearly monetary stipend was not an “employee” and could not bring sex and age discrimination lawsuit under KCRA.

3. Definition of “Retaliation”

- a. KRS §344.280 makes it an unfair employment practice for an employer to “retaliate or discriminate in any manner against a person because he has opposed a practice declared unlawful by this chapter, or because he has made a charge, filed a complaint, testified, assisted, or participated in any manner in any investigation, proceeding, or hearing under this chapter”
- b. In Bank One, Kentucky v. Murphy, 52 S.W.3d 540 (2001), a former employee, who had brought suit against her employer for sexual harassment, alleged that the employer violated KRS §344.280 because it filed a declaratory action (during on going settlement negotiations) in the U.S.

District Court seeking a determination that it was entitled to prevail on its affirmative defenses under the U.S. Supreme Court's decisions in Burlington Industries v. Ellerth, 524 U.S. 742 (1998) and Faragher v. City of Boca Raton, 524 U.S. 775 (1998).

The Court rejected the plaintiff's contention that filing a suit while settlement negotiations were on-going was retaliatory in nature. "While it may amount to bad manners or may appear to some to be unprofessional, such conduct does not constitute a violation of the statute nor is it tortious."

4. Election of Remedies

- a. Doctrine of "election of remedies" means that if a person has two modes of legal redress for an injury suffered which are contradictory and inconsistent with each other, the deliberate and settled pursuit of one will preclude a later choice to pursue the other.
- b. KRS §342.690(1) provides that a claim for workers' compensation benefits is "exclusive and in place of all other liability of such employer to the employee" Subsection (4) creates an exception to this "exclusive remedy" rule if the employee is injured through the deliberate intention of the employer.
- c. In American General Life & Accident Insurance Company v. Hall, 2002 WL 442044 (Ky. March 21, 2002) an employee sued her employer for damages for mental and emotional injuries inflicted by the employer's sexually discriminatory practices. The employee accepted workers' compensation benefits for "psychological problems resulting from sexual harassment" by her immediate supervisor. The Court concluded that because the Plaintiff's workers' compensation claim and her civil rights claim were premised upon the same injury (harassment by her supervisor) and the same resulting damages, she was only entitled to only one remedy (workers' compensation award she had previously accepted).
- d. In Wilson v. Lowe's Home Center, 2001 WL 1658212 (Ky.App. Dec. 28, 2001) the Court held that an employee who initially opted to use the administrative process provided under KCRA for redress of his charge of race discrimination and hostile work could withdraw his complaint before the Kentucky Commission on Human Rights prior to a final determination on the merits and to subsequently file a discrimination complaint in circuit court.

5. Extraterritorial and Intraterritorial Application of Civil Rights Statutes

a. In Union Underwear Company, Inc. v. Barnhart, 50 S.W.3d 188 (Ky. 2001), the Kentucky Supreme Court was asked the question whether a Georgia employee of a New York corporation that had its headquarters in Kentucky could bring suit under KCRA for age discrimination when all acts of alleged discrimination occurred outside of Kentucky and the employee never lived and worked in Kentucky.

i. There is a well-established presumption against extraterritorial operation of statutes. Thus, unless a contrary intent appears within the language of the statute, courts presume that the statute is meant to apply only within the territorial boundaries of the Commonwealth.

ii. KCRA does not contain any express provision for the extraterritorial application of KCRA. Nothing in the act implies that it was intended to operate beyond Kentucky's borders. There is express language to the contrary. The purpose of KCRA is described as one to "safeguard all individuals *within the state* from discrimination"

iii. KCRA has no extraterritorial application. In accord, Equal Employment Opportunity Commission v. Arabian American Oil Co., 499 U.S. 244 (1991)(Title VII does not apply extraterritorially to regulate employment practices of United States employers who employ United States citizens abroad.)

b. In Rogers v. Fiscal Court of Jefferson County, 48 S.W.3d 28 (Ky.App. 2001), the Court was faced with the question whether the Jefferson County ordinance prohibiting sexual orientation and gender identity discrimination in employment, public accommodations and housing could be enforced in the City of Louisville which had adopted an ordinance that prohibited sexual orientation and gender identity discrimination in just employment.

i. K.R.S. §67.083(7) provides that : "County ordinances which prescribe penalties for their violation shall be enforced throughout the entire area of the county unless: (a) Otherwise provided by statute; or (b) The legislative body of an city within the county has adopted an ordinance pertaining to the same subject matter which is the

same as or more stringent than the standards that are set forth in the county ordinance.

- ii. Because of the express statutory command and the lack of applicability of the exemptions contained within the statute, the Court held that the more expansive county civil rights statute was enforceable within the City of Louisville.



**THE AMERICANS WITH DISABILITIES ACT:
AN ANALYSIS OF RECENT DECISIONS**

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SECTION B



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THE AMERICANS WITH DISABILITIES ACT: AN ANALYSIS OF RECENT DECISIONS

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I. INDIVIDUAL WITH A DISABILITY

- Toyota Motor Manufacturing, Kentucky, Inc. v. Williams, 534 U.S. ___, 122 S.Ct. 681 (January 8, 2002).

The United States Supreme Court recently overturned the Sixth Circuit Court of Appeals decision and held that in order for an individual to be substantially limited in the major life activity of performing manual tasks, she “must have an impairment that prevents or severely restricts the individual from doing activities that are of central importance to most people’s daily lives.” The court noted that these activities would include attending to one’s personal hygiene and performing various household chores. Contrary to plaintiff’s position, it did not include an individual’s ability to perform “repetitive work with [her] hands and arms extended at or above shoulder levels for extended periods of time,” since these duties were not central to most people’s daily lives. The United States Supreme Court rejected the Sixth Circuit’s finding that a worker will be considered disabled if an impairment substantially limits her ability to perform a class of job-related manual tasks. The Supreme Court holding restricts the application of the ADA; whether it will limit disability discrimination litigation in the future remains to be seen.

Plaintiff was hired by defendant Toyota Motor Manufacturing Company in 1990 to work in the paint department. She was later assigned to a position on the engine fabrication assembly line which required her to use pneumatic tools. Plaintiff was subsequently diagnosed with carpal tunnel syndrome. To accommodate plaintiff’s medical restrictions she was assigned a variety of modified-duty jobs over the course of a two year period.

Plaintiff was eventually placed in a quality-control position, which duties included visually inspecting painted cars moving down the assembly line for imperfections. In 1996, the Company decided that all quality-control employees must rotate through a variety of tasks such as wiping oil on the cars’ hood, fenders and doors. These duties required plaintiff to hold her hands and arms around shoulder height for several hours at a time.

Plaintiff began experiencing pain in her neck and shoulders and requested to be excused from having to perform these functions and return to the paint inspection job full-time. The Company rejected plaintiff’s request because these duties were determined to be within her restrictions. Plaintiff contends that she was forced to perform the wiping duties that aggravated

her condition, which subsequently led to her doctor directing her to avoid all work-related activities for a period of time. Soon thereafter, plaintiff was terminated based on her poor attendance record.

Plaintiff filed a disability discrimination action alleging that the Company violated the ADA by failing to reasonably accommodate her and terminating her employment. The district court granted summary judgment in the Company's favor finding that plaintiff was not disabled because she was not substantially limited in the major life activities of lifting, performing manual tasks or working. In reaching this conclusion, the lower court judge noted that plaintiff was able to engage in "personal hygiene activities" and carry out household chores despite her alleged condition.

The case was appealed to the Sixth Circuit Court of Appeals, which disagreed with the lower court's findings and reversed the summary judgment. The Sixth Circuit Court of Appeals held that Williams' condition prevented her from doing the tasks associated with "certain types of manual assembly line jobs, manual product handling jobs, and manual building trade jobs (painting, plumbing, roofing, etc.) that required the gripping of tools and repetitive work with hands and arms extended at or above shoulder levels for extended periods of time." The United States Supreme Court accepted this case to decide the proper standard for determining whether an individual is substantially limited in performing manual tasks.

The high court held that an individual seeking to prove that she is substantially limited in the major life activity of performing manual tasks must first demonstrate that the manual tasks involved are "of central importance to people's daily lives." Additionally, the court held that "the impairment's impact must be permanent or long term." Because most people are not required to be able to "perform repetitive work with [their] hands and arms extended at or above shoulder levels for extended periods of time," the inability to do so in and of itself is insufficient to constitute a substantial limitation on a major life activity of performing manual tasks. Further, the court emphasized that these standards must be applied on a case-by-case basis.

Of significant importance, the Supreme Court highlighted the Sixth Circuit's failure to focus upon Plaintiff's ability to perform personal hygiene and household chores. The court noted that activities such as bathing and brushing one's teeth are "the types of manual tasks of central importance to people's daily lives." Since plaintiff admittedly could perform these tasks, her limited impairment in other areas of her life were not sufficiently severe to establish a manual task disability. By requiring plaintiffs to prove that the manual task in which they are limited is "central to most people's daily lives" it may create more difficult standard for a plaintiff to prove that they are disabled under the ADA.

- Swanson v. University of Cincinnati, 268 F.3d 307 (6th Cir. 2001).

The Sixth Circuit held that an employee was not substantially limited in a major life activity when the duration of his depression was short. Plaintiff began his surgical residency at the University of Cincinnati ("UC") on July 1, 1995. During his residency his performance began to decline and in May, 1996 he was placed on academic probation until September, 1996. In May and June his performance continued to drop. Based on the recommendation of another

physician plaintiff had seen, plaintiff sought psychiatric treatment in July, 1996. He was diagnosed with major depression and began taking medication. Plaintiff's performance began to improve, however, one of plaintiff's evaluators suggested he transfer to another residency besides surgery.

On October 31, 1996 Plaintiff was terminated from his residency position. He requested to be reinstated, receive a leave of absence and/or some accommodation, but each request was denied. Plaintiff subsequently filed a lawsuit alleging disability discrimination against his employer, UC.

The employer argued that plaintiff's major life activities were not substantially limited by his condition because his restrictions were short term and improved with medication. The Sixth Circuit Court of Appeals agreed with the employer's position that although plaintiff's depression affected his ability to concentrate, it did not significantly restrict it. Nor was plaintiff's sleep or communication significantly restricted since with medication he continued to have future success. Plaintiff's impairment was short-term because with medication he improved significantly. Thus, the court noted, that an employer must consider the duration of an otherwise substantially limiting impairment when they are determining whether an individual is disabled under the ADA.

- Chenoweth v. Hillsborough County, 250 F.3d 1328 (11th Cir. 2001).

The Eleventh Circuit held that an inability to drive to work for six months does not qualify as an impairment that substantially limits a major life activity. After the employee was diagnosed with focal onset epilepsy, her doctor advised her not to drive until she had gone six months without experiencing a seizure. Employee's position as a nurse involved driving between different sites where she carried out file reviews. The employee asked to work at home and for a variable schedule to accommodate her transportation needs. The employer eliminated the requirement that she drive between work sites, but denied the other requests. The Eleventh Circuit held that the ability to drive to work is not a major life activity, noting that it requires a license from the State that can be revoked for a number of reasons, such as failure to insure, and that millions of individuals are not self-driven to work. Further, the court concluded that there was no evidence in the record that the employee's inability to drive substantially limited her ability to work.

- Contreras v. Sun Coast Corp., 237 F.3d 756 (7th Cir. 2001).

The Seventh Circuit held that a forklift operator's inability to lift more than 45 pounds for a long period of time, to engage in strenuous work, or to drive a forklift for more than four hours per day did not constitute a substantial limitation on his ability to work, absent a showing that he was precluded from a broad class of jobs. The Court also concluded that the employee's inability to engage in sexual intercourse more than twice per month due to his back injury did not substantially limit the major life activities of reproduction or engaging in sexual relations. Although the employee claimed that he was able to have intercourse 20 times per month prior to his injury, he failed to present any evidence regarding the condition, manner or duration of his inability to reproduce as compared to the average person in the general population.

- EEOC v. United Parcel Service Inc., 249 F.3d 557 (6th Cir. 2001).

The Sixth Circuit held that a delivery driver who suffered a severe reaction to an allergen (pollen of a Mountain Cedar plant) specific to Central Texas had made a *prima facie* showing that he was disabled. The driver resigned his employment after the employer denied his request for a transfer to Ohio. Although the employee could still perform the essential functions of his job at the time that he requested the transfer and his reaction to the allergen cleared up after he moved, his reactions to the allergen were steadily worsening at the time of his transfer request.

The plaintiff employee rarely left home during his non-working hours, his wife took care of his household duties, and the employee suffered from severe nasal and bronchial congestion, swollen eyes and nose, rashes, fever blisters, fatigue, fever and depression. His physician stated that effective allergy medication would threaten the employee's safe operation of a truck. The court therefore concluded that a reasonable jury could find that the employee was disabled because his allergies substantially limited his ability to do his job while in Texas. The court also held that a reasonable jury could conclude that the employee's resignation was not voluntary, but an involuntary loss of his job due to the employer's failure to reasonably accommodate his disability.

- Tangires v. Johns Hopkins Hosp., 79 F. Supp. 2d 587 (D. Md. 2000), aff'd 230 F.3d 1354 (4th Cir. 2000).

Plaintiff's asthma was found not substantially limiting because it was correctable by medication, even though the plaintiff refused to take the medication. Plaintiff's doctor testified that her asthma was slow to clear because she refused to comply with his recommendations and was reluctant to take steroid drugs. The court concluded that because Plaintiff's asthma was correctable by medication and she voluntarily refused the medication, she was not substantially limited in a major life activity.

II. "REGARDED AS" DISABLED

- EEOC v. Rockwell Int'l Corp., 243 F.3d 1012 (7th Cir. 2001).

The Seventh Circuit Court of Appeals held that the EEOC failed to prove that the defendant Company discriminated against prospective employees in failing to hire them based solely on the results of a nerve conduction test that identified people susceptible to neuropathy. While the applicants did not presently have an impairment at the time the Company failed to hire them, the EEOC argued that the defendant regarded them as disabled. The Seventh Circuit disagreed, holding that the Company regarded the applicants as unable to perform only four specific jobs in the workplace and that the record contained no evidence that the applicant's perceived inability to perform jobs requiring frequent repetition or use of vibratory power tools precludes them from any other jobs in the geographic area.

Moreover, the court rejected the Company's argument that in the context of proving a substantial limitation in the major life activity of working, a plaintiff must always present

quantitative evidence of the characteristics of the local job market, and number and types of jobs from which he or she is precluded. The court noted that in some rare cases the impairments are so severe that substantial foreclosure from the job markets is obvious. In other cases, however, a plaintiff must present some evidence of the number and types of jobs for which he or she is precluded because of a disability (or perceived impairment), and/or demographics of the relevant labor market.

- Henderson v. Ardco Inc., 247 F.3d 645 (6th Cir. 2001).

Plaintiff employee brought an action against her former employer alleging disability discrimination among other claims because the employer's policy prohibited her from working unless she was "100% healed." The Sixth Circuit Court of Appeals held that the employer's "100% healed" policy was evidence that she was "regarded as" disabled.

Plaintiff employee was on a medical leave for seven months recuperating from an injury. When the employee returned to work she had several physical restrictions. The Company's manager refused to allow the employee to return to work stating that the Company had a policy that she must be "100% healed." The Company's policy was well known and consistently applied.

The employee requested the Company accommodate her restrictions and was informed that the Company had no light duty work that she could perform with her current medical restrictions. The Court of Appeals allowed the employee to proceed with her claim of disability discrimination based upon the Company's statement that "there is not a job in this plant that [plaintiff's] restrictions would not bump into." The court believed this statement could be interpreted as indicating that the Company believed the employee was unable to do any factory work and such broad scope of an employee's perceived disability could constitute disability discrimination, if proven.

- Ross v. Campbell Soup Co., 237 F.3d 701 (6th Cir. 2001).

The Sixth Circuit held that the plaintiff employee presented sufficient evidence to create a factual dispute as to whether the defendant employer regarded him as being disabled. The evidence presented included: (1) Comments in a memo regarding whether the employee should be given a bonus which referred to the employee as a "problem person" and which had a post-script stating "back case"; (2) supervisor's remark to employee that "we can't have any more of this back thing"; (3) supervisor's completing a "Job Accommodation Request Analysis" despite the fact the employee did not request an accommodation and indication on such form that the supervisor consulted with the medical department to determine the employee's condition was a disability rather than a temporary impairment; and (4) supervisor's testimony regarding the plaintiff employee's back trouble that stated "there are certain things that will raise red flags to you that require a person be given, maybe, a little extra benefit of a doubt."

III. QUALIFIED INDIVIDUAL WITH A DISABILITY

- Bay v. Cassens Transport Co., 212 F.3d 969 (7th Cir. 2000).

The Seventh Circuit Court of Appeals held that a truck driver was not a “qualified individual” under the ADA when he did not possess the certification required by the Department of Transportation (DOT). DOT regulations prohibited an employer from permitting a driver to resume driving until he produced a doctor’s certification indicating that he was physically qualified to drive. The Seventh Circuit indicated that it would not examine the medical basis for the physician’s refusal to provide the certification absent evidence that the employer attempted to prevent the employee from being recertified, acting in bad faith, or unreasonably relied on the physician’s medical determination. The Seventh Circuit further indicated that a court may examine the underlying medical basis when the decision is based on a condition not covered by DOT regulations, the driver’s lack of certification is a pretext for discrimination or if an employer is working in collusion with a medical professional to deny certification.

- Kiphart v. Saturn Corp., 251 F.3d 573 (6th Cir. 2001).

The Sixth Circuit Court of Appeals affirmed a jury’s finding that being a fully rotational team member of an automotive assembly team was not an essential function of the team member’s job. Some job announcements did not list the ability to rotate fully as a necessary qualification and there was evidence that the only time the employer fully implemented the job rotation requirement was when it placed employees with job restrictions.

- Basith v. Cook County, 241 F.3d 1919 (7th Cir. 2001).

The Seventh Circuit held that delivering and stocking of medications were essential functions of a pharmacy technician’s job in a county hospital. In coming to this conclusion, the Seventh Circuit held that a court may consider, but is not limited to, evidence regarding an employer’s judgment of the position, written job descriptions prepared for advertising or interviewing applicants, and the work experience of past and current employees in that position. Moreover, the Court held that one must determine whether an employer actually requires all employees in a particular position to perform the allegedly essentially job functions, but should not otherwise second-guess the employer’s judgment. For an employee to overcome deference to the employer’s judgment, the employee must offer sufficient evidence that the employer’s understanding of the essential job functions is incorrect. Further, while the amount of time the function encompasses is evidence whether the function is essential, the function need not encompass a significant amount of time in order to be essential. The mere fact that other employees are available to perform the function also does not render the function non-essential.

In this case, while the technician’s delivery of medications only took 45 minutes of an eight hour day and other employees could have delivered the medication, delivery of medication is essential to the pharmacy’s functions and the employer determined that the technician position was the best position to fulfill this vital duty. In determining that the functions were essential, the court relied upon the employer’s “Essential Job Function Form,” which predated the employee’s injury, was completed by six other pharmacy employees, and listed the work

experience of current and past employees in the technician position. Additionally, the court noted that the fact the employer had gone beyond the requirements of the ADA and created a special assignment for the technician which did not require delivery of medication was not proof that delivery of medication was non-essential, absent other independent evidence. The court deemed that holding otherwise would have punished the employer for going beyond the requirements of the ADA.

IV. REASONABLE ACCOMMODATION

- U.S. Airways, Inc. v. Barnett, ___ U.S. ___, No. 00-1250 (decided April 29, 2002); U.S. Airways, Inc. v. Barnett, 228 F.3d 1105, vacated and remanded.

The United States Supreme Court held that an employer's showing that a requested accommodation conflicts with seniority rules is ordinarily sufficient to show, as a matter of law, that an "accommodation" is not "reasonable." However, the employee remains free to present evidence of special circumstances that makes a seniority rule exception reasonable in the particular case.

Plaintiff employee injured his back while working for U.S. Airways, Inc. as a cargo handler. After his injury, he transferred to a less physically demanding mailroom position. The mailroom position later became available to seniority-based employees bidding under the employer's seniority system. Employees senior to plaintiff planned to bid on the mailroom job. Plaintiff requested to remain in the mailroom position as a reasonable accommodation to his disability, however the employer refused and plaintiff lost his job. Plaintiff filed suit under the ADA alleging that his former employer discriminated against him by not providing him a reasonable accommodation of the job transfer.

The ADA prohibits an employer from discriminating against "an individual with a disability" who with "reasonable accommodation" can perform a job's essential functions, unless the employer "can demonstrate that the accommodation would impose an undue hardship on the operation of [its] operation of business." See 42 U.S.C. §12112(a) and (b) and §1211(b)(5)(A). The district court held that altering a seniority system would result in an "undue hardship" to the employer and its non-disabled employees and therefore granted the Company summary judgment. The Ninth Circuit Court of Appeals reversed the lower court's holding that "the seniority system was merely a factor in the undue hardship analysis and that case-by-case, fact intensive analysis is required to determine whether any particular assignment would constitute an undue hardship." Due to conflicting holdings between the circuits, the United States Supreme Court agreed to hear the case.

The U.S. Supreme Court's plurality opinion held that generally an employer's proof that a requested accommodation conflicts with seniority rules is ordinarily sufficient to show that an "accommodation" is not "reasonable." However, the plaintiff employee may present evidence of special circumstances that makes a seniority rule exception reasonable in the particular case and therefore overcome summary judgment. Id. at p. 4-15.

Justice O'Connor's concurrence opinion would limit the seniority system defense to only those cases involving "enforceable" seniority rights. In O'Connor's view, the plurality opinion will be interpreted by the lower courts to require a showing of enforceability as a prerequisite to successful defense that seniority rules render a requested transfer as "unreasonable."

- Burns v. Coca Cola - Enterprises, Inc., 222 F.3d 247 (6th Cir. 2000).

The Sixth Circuit Court of Appeals held that an employee was disabled under the ADA in part because his "personal education and prior work experience" limited his ability to pursue employment in other sectors of the economy. The Sixth Circuit believes that an individual may be deemed disabled within the meaning of the ADA merely because he has a physical or mental impairment that becomes substantially limiting when considered with factors such as work experience and education.

Additionally, this case is important because the employer had a documented policy requiring all employees seeking transfers to file a written "Request for Transfer" form. The plaintiff employee did not follow Company policy in completing the form. Therefore, the employee was not transferred into a position notwithstanding his contention that jobs were available for which he was qualified and that he should have been allowed to transfer into one of those positions. Due to the plaintiff's failure to comply with Company policy, the court held he could not claim that the employer failed to accommodate him under the ADA.

- Hoskins v. Oakland County Sheriff's Department, 227 F.3d 719 (6th Cir. 2000).

The Sixth Circuit Court of Appeals reinforced the well-settled law that an employer does not have to create a new job as a reasonable accommodation for an employee. Plaintiff was a sheriff's deputy who could not perform the duties involved in her position because of her alleged disability. Therefore, plaintiff requested a transfer to a position in the jail's control booth. A control booth operator's primary duties include allowing other officers to enter and leave the cellblocks. Historically, the position of the control booth operator was delegated to each of the deputy sheriffs on a rotating basis to allow them a break from their more stressful and physically demanding sheriff's deputy job duties. The court held that plaintiff's requested accommodation to a permanent position of a control booth operator was unreasonable under the ADA since it would essentially create a new job.

- Garcia-Ayala v. Lederle Parenterals, Inc., 212 F.3d 638 (1st Cir. 2000).

The First Circuit held that the lower district court erred when it concluded that an additional five-months of unpaid leave beyond the one-year leave provided under the employer's leave policies was not a reasonable accommodation, based on its conclusion that the district court failed to perform an individualized inquiry and seemed to be fashioning a *per se* rule. The First Circuit noted that in some circumstances such a lengthy leave may be unreasonable, however the facts in this particular case did not warrant such a finding.

In this case, during the plaintiff's absence, her employer filled her secretarial position with individuals hired from temporary agencies. Plaintiff did not request pay beyond the

disability benefits provided by the employer and there was no evidence in the record to suggest that the temporary employees were being paid more than the plaintiff or were less effective in the job than plaintiff had been. Therefore, the court concluded that there appeared to be no business pressure to fill the secretarial position with another permanent employee, and in fact, the employer never did so. Thus, under these particular circumstances, the additional leave request was reasonable.

- Walsh v. United Parcel Service, 201 F.3d 718 (6th Cir. 2000).

The Sixth Circuit held that an employer did not violate the ADA in denying an employee's request for additional leave in order to obtain a medical diagnosis. The employee had sufficient time to obtain a medical diagnosis and provide the employer information concerning his condition when he received a year's paid leave following an accident-related disability, and six months of unpaid leave following the expiration of his paid leave. When the employee failed to provide the information requested, the Company terminated the employee.

V. DIRECT THREAT DEFENSE

- Chevron U.S.A., Inc. v. Echazabal, 213 F.3d 1098 (9th Cir. 2000), amended 226 F.3d 1063 (9th Cir. 2000), cert. granted October 29, 2001.

The Ninth Circuit Court of Appeals held that the ADA's "direct threat" defense is permissible only when an employer denies employment when an employee's condition threatens the health or safety of others in the workplace. In 1972, plaintiff was employed by maintenance contractors who performed work at Chevron's Oil Refinery. Plaintiff was exposed to solvents and chemicals in that position. In 1992, he applied to work directly for Chevron. While the Company determined he was qualified for the job, a pre-employment physical revealed his liver was releasing certain enzymes at a larger than normal level. Due to the physical examination results, Chevron determined that plaintiff's liver may become damaged if he continued to work in the coker unit where he was exposed to harmful solvents and chemicals. Chevron withdrew its offer of employment to plaintiff.

Plaintiff continued to work for the independent maintenance contractor in the same position in the coker unit and Chevron made no attempts to remove him from that position. In 1995, plaintiff applied to Chevron for a position in the coker unit. Again, Chevron made a job offer to plaintiff contingent upon passing a physical examination. Chevron withdrew its job offer following plaintiff's physical examination when it revealed that his liver may be damaged if he worked in the coker unit. Unlike in 1992, Chevron wrote plaintiff's employer and requested that he immediately be removed from the position to eliminate his exposure to the chemicals. The independent contractor removed the plaintiff from his position at Chevron. Plaintiff soon thereafter filed a lawsuit against Chevron and his previous employer claiming they discriminated against him on the basis of a disability in violation of the ADA, among other claims.

Chevron argued that it was not required to hire plaintiff and was permitted to request his removal from the refinery in his independent contractor's position since his continued presence

would pose a direct threat to his own health. "Direct threat" is defined in the ADA as a "significant risk to the health or safety of others that cannot be eliminated by reasonable accommodation." Therefore, the Court rejected Chevron's argument. The Court further stated in its Opinion that the ADA's legislative intent reflects that "employers may not deny a person unemployment opportunity based on paternalistic concerns regarding the person's health." Thus, an employer may not lawfully deny an individual employment when the job duties or work environment pose a risk of injury or illness to the individual. Due to conflicting opinions in other federal appellate courts, the United States Supreme Court granted review of this decision.

VI. CAUSAL CONNECTION REQUIRED IN ADA CASES

- Parker v. Sony Pictures Entertainment, Inc., 260 F.3d 100 (2nd Cir. 2001).

The Second Circuit Court of Appeals held that when an employee with a disability is injured by the employer's failure to provide a reasonable accommodation, no additional showing of animus against persons with disabilities is required to establish ADA liability. However, in order to find an employer liable under the ADA, there must be a connection between the employer's failure to accommodate a disability, the employee's performance deficiencies and the adverse employment action. The employee plaintiff must further prove that protected characteristics "played a motivating role in, or contributed to, the employer's decisions." The "motivating factor" requirement would be satisfied when: (1) both the lack of an accommodation and some other factor plays a role in the employee's failure to return to work or (2) when both the failure to return to work and some other factor played a role in the employer's termination decision.

In Parker, plaintiff employee sued his employer after being fired when he did not return from a six month medical leave of absence. The employer argued that it believed the former employee was not able to return to work and that he never requested an accommodation. The employer based its belief upon the employee's submission of several medical reports for their long-term disability benefits and Social Security Disability Insurance in which the employee claimed he was unable to work and was completely incapacitated. Despite those reports, the employee claimed that he told the employer that he would be able to return to work if they accommodated him with a modified schedule. Subsequent medical reports indicated that the former employee's condition was unchanged and therefore they did not suggest whether he could return to work and did not mention any work restrictions.

While the employee asserted that the employer violated the ADA by failing to provide a reasonable accommodation, which he needed in order to return to work, the jury found the employee failed to show a causal connection between his disability and his termination. While the jury found that the employee had a disability, could not perform the essential functions of his job without a reasonable accommodation, could perform the essential duties with a reasonable accommodation, requested a reasonable accommodation and such accommodation would not have imposed an undue hardship on the Company, the jury concluded that the employer did not know that the employee could perform the essential functions of his job with a reasonable accommodation. Therefore, the employee's disability was not a motivating factor in the employer's decision to discharge him.

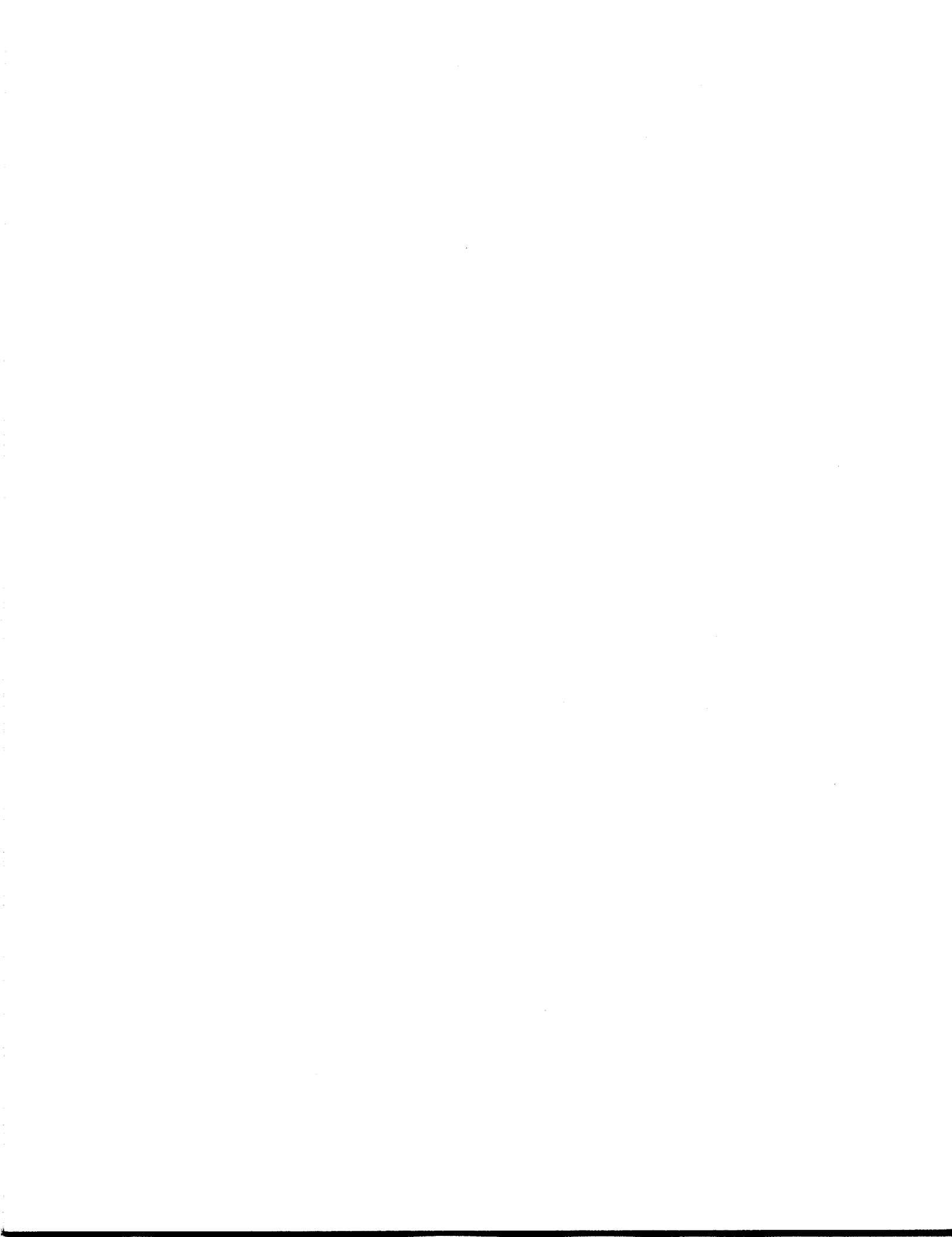
**LITIGATION TACTICS:
THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE**

Plaintiff's Perspective

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**LITIGATION TACTICS:
THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE**

FROM THE PLAINTIFF'S PERSPECTIVE

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SECTION C(a)



**LITIGATION TACTICS: THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE**

From The Plaintiff's Perspective

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**LITIGATION TACTICS: THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE
FROM THE PLAINTIFF'S PERSPECTIVE**

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I. INTRODUCTION.

This outline addresses two of the most crucial tactics the Plaintiff's employment litigator should employ for ultimate success:

1. *A well devised strategy and story plan;*
2. *Evaluating, engaging, and endearing the jury.*

II. DEVISING THE STRATEGY AND DEVELOPING YOUR STORY PLAN THROUGH DISCOVERY.

A. *DEVELOP THEORY OF THE CASE AND CASE PLAN.*

Establish the legal objectives of your case.

Before you take the first step into the discovery realm of your case, you must outline your legal goals - how will you "prove-up" your case for the jury? The most fatal mistake for a beginning practitioner in a discrimination case is to jump into the discovery process without such defined legal objectives, allowing the defendant corporation to lead the plaintiff's attorney on a lengthy and expensive fishing expedition, which neither the plaintiff nor her attorney can afford.

1. **Identify the elements of proof required to support *each legal claim.***

Start by reviewing each of the legal claims set out in your Plaintiff's Complaint. Reviewing the individual legal elements of these claims, draft a proposed jury instruction for each. These jury instructions will be the basis for the *liability* aspect of your case objectives, which will represent the first half of your discovery plan.

2. Identify the elements of proof required to support your damages.

The second portion of your legal objectives is based on the damages aspect of your claim. Many litigants fail to recognize the importance of damages proof until just before trial. This can be quite tragic to your case if a component of damages requires some element of proof from defendants, such as payroll records or benefit plan descriptions.

Outline each of your damage claims, specifically identifying the elements of proof for each. This plan, combined with the legal elements plan, completes the legal objectives portion of your entire case plan.

Outline the factual theories to support each legal objective.

1. Create your factual plan.

After combining the damages and liability portion of your legal objectives, it is time to determine the facts you will need to support these claims.

The very basic difference between a winning discrimination claim and a failed one is the strength of the factual support for the discriminatory animus. This support can only be assimilated through discovery of the defendant employer and its agents and managers.

Thus, you should build your factual support by formulating a detailed outline within each of your legal objectives. An example of how you would build your claim of quid pro quo sex discrimination follows:

B. PRACTICE SAMPLE: LEGAL OBJECTIVES AND FACTUAL THEORIES

Goal of Proof: Quid pro quo sex discrimination by a supervisor.

First: Set out elements of proof for your legal claim:

1. Proof of a sexual advance.
2. By a supervisor.
3. Promise of job security, advancement, or other benefit.
4. Employer's knowledge.
5. Employer's failure to act.
6. Damages to Plaintiff.

Second: Set out factual requirements to meet the legal proof:

1. Proof of a sexual advance.
 - Plaintiff's testimony.
 - Witness A's testimony of harasser's advance to her.
 - Employer's record of investigation of witness A's complaint.

- Harasser's testimony.
2. "By a supervisor."
 - Plaintiff's testimony that she understood harasser to be her boss.
 - Personnel file of harasser.
 - Other witnesses to establish supervisor duties of harasser.
 3. Promise of job security, advancement, or other benefit.
 - Plaintiff's testimony.
 - Witness B's testimony.
 - Plaintiff's personnel file.
 - Job postings.
 - Policies and procedures manual.
 4. Employer's knowledge.
 - Plaintiff's testimony.
 - Employer's records of investigations.
 - Personnel file of harasser.
 - EEO Charges.
 - Testimony of witnesses A and B.
 - Policies and procedures.
 5. Employer's failure to act.
 - Plaintiff's testimony.
 - Policies and procedures.
 - Records of this complaint and others.
 - Testimony of witnesses A and B.
 6. Damages to Plaintiff.
 - Plaintiff's testimony.
 - Employer's benefit plan packages.
 - Plaintiff's personnel file.
 - Testimony of HR manager (wage and benefit loss).
 - Testimony of "before and after" witnesses (emotional distress).

Gather all the information in Plaintiff's possession, and any other available to Plaintiff.

Obtain and compile every bit of information which your plaintiff has in her possession, or that which is immediately available to her. Make sure you specifically review with her your factual needs, e.g. the employer's policies and procedures (does she have a copy of the policy handbook?; can she easily obtain a copy from another former employee, or from a box in her own garage?).

Next, discuss her ideas for some good sources for other factual needs, specifically the identity of witnesses. Determine the best approach for contacting non-

employer witnesses, and to what extent plaintiff should be involved. As a general rule, if the plaintiff is willing and able to make the first contact with a lay witness, the witness is generally more cooperative and can become a strong ally in the development of the case. Potential witnesses who are initially approached by an attorney in these highly sensitive situations are sometimes “gun shy” about testifying. The plaintiff can thus play an important role in merely “introducing” the lay witness to the background of the case and to the attorney.

Finalize your “plan” by determining what other information is still outstanding.

Discovery is the process by which you fill the open spots on your case plan that have not been filled by information your plaintiff has provided.

Begin with the information you can acquire from other witnesses not associated with the employer - friends, relatives and acquaintances of plaintiff who can informally provide you with both substantiating and new information about your client’s case.

Once you have the entire plan together, identify which information you will require from employer, and move to the “tools of discovery” to obtain it.

C. CONTROL DEFENDANT’S “BLANKET” ACCESS TO YOUR CLIENT’S RECORDS.

1. Access to your Plaintiff’s medical/mental records.

When it appears that an FRCP 35 motion for the plaintiff’s medical/mental records will be requested by defendant, plaintiff should always consider moving the court to limit such motion to the proper scope. The proper scope of such a motion is largely dictated by the type of discrimination the plaintiff suffered, and her theory for damages.

If the plaintiff was discriminated against due to a disability, the scope of relevant medical records is likely to be much more broad. The defendant usually has the right, at a minimum, to look as far back as the disability goes.

Scope truly comes into play, however, when the plaintiff is claiming damages due to emotional distress. Frequently, no medical records will exist for proof of such emotional distress, and it must be proved through other factual means. As the claim for emotional distress is alleging the distress as a result of the plaintiff’s employment, the plaintiff should attempt to limit scope for mental records to the duration of employment.

2. Access to a medical/mental examinations on Plaintiff.

Medical and mental examinations may be introduced only upon order of the court, and can only compel a party to the action. FRCP 35 provides that the physical or mental condition to be examined must not only be relevant to the action, but also in controversy. A court will consider a number of factors in determining good cause for an order for a medical or mental exam.

Plaintiff's attorney should pay particular attention to motions for medical and mental exams as they hold great potential for revealing circumstances which, even if irrelevant to the case at hand, could nonetheless negatively affect the outcome of plaintiff's case.

Motions for medical and mental examinations are frequently made in employment discrimination cases, as very often the plaintiff's medical or mental condition is at issue. Review any such motion for adherence with the "in controversy" and "good cause" elements described in FRCP 35, and formulate any available argument in opposition to the motion.

Schlagenhauf v. Holder, 379 U.S. 104 (1964). (This is a case of long-standing importance, stressing the focus of the "in controversy" and "good cause" factors.)

III. VOIR DIRE: IMPLEMENTING YOUR STRATEGY AND SERVING THE TRUTH AT TRIAL.

A. *MAKE YOUR BEST EFFORTS TO ENGAGE THE JURY.*

Once the Plaintiff's employment attorney gets to trial, the most important litigation tactic, other than the presentation of your Plaintiff's "story" in direct examination, is **voir dire**. Since the jurors "are the law" for the purposes of your trial, you need to know how your jurors "tick" before you approach and convince them of your client's story.

The first idea you must solidify in the minds of the jurors is that *this is the most important day in your client's life*. Further, *they are the most important people to help him/her*.

What is it that you really need to know to understand where each of your jurors stand, and how to make them focus on your client? As Phillip C. McGraw, Ph.D. wrote in his #1 New York Times Bestseller, "*Life Strategies: Doing What Works, Doing What Matters*", "[I]f you want to genuinely know what someone or some group is really all about", you ask the following questions:

- 1 - What do they value most in their lives: Are ethics a big deal? Do money and success define them? Do they value strength, or compassion? What really matters in their outlook on life?
- 2 - What are their expectancies and beliefs about how life does and should work?
- 3 - What resistances or predispositions - fears, biases, prejudices - do they have?
- 4 - What positions or approaches or philosophies are they most likely to reject or accept?
- 5 - What do they need to hear from a person in order to conclude that that person is fundamentally 'okay' and to be trusted?
- 6 - What sorts of things do they consider relevant?
- 7 - How do they feel about themselves?
- 8 - What do they want most in their lives?

These are the exact questions you need to formulate to approach a jury. Rewrite these questions, of course, to match the specific facts of your case, the peculiarities of your client, and the issues that relate to her story. The answers can be used to *cement* your previously established strategy and help you present your client in the most compelling but favorable light.

B. COMBATING JUROR BIAS: BE VIGILANT TO THE SKEPTICISM.

What constitutes an "impartial jury" and a "fair trial"? The ultimate hope is that jurors come to the Court with a *clean slate* to be filled with only that information entered into evidence.¹ But if we stop for a moment to think about the extensive prejudices each of us has developed just in the last six (6) months due to changes occurring in our society as a whole, is there any doubt that similar prejudices have occurred within the personal lives of every person who sits on a jury? If each of us, as an advocate, trained under the notion that "justice is blind" is subject to such bias, how could we expect any juror to enter the courtroom with a "clean slate"? Add to these prejudices the saturation of news influencing our society, the talking heads on the various legal dramas broadcast everyday, and the increasing skepticism toward the legal

¹ Steven I. Friedland, *Legal Institutions: The Competency and Responsibility of Jurors in Deciding Cases*, 85 Nw. U.L. Rev. 190, 1990.

process, and we must know the real truth - every jury room in this country is "full up" with prejudice and bias.

C. PUT YOUR KNOWLEDGE TO WORK: ENDEAR THE JURORS.

The task of addressing juror biases is two-fold. First, there is the classic challenge of eliminating the most biased jurors during voir dire. Although it does not clean the slate, it hopefully creates more of a balance among those to be selected. Second, is the task of adjusting the trial approach *toward* the prejudices of the jurors finally seated, and win them over!

In an employment discrimination case, this second stage of "transforming" the jurors' attitudes to a client's advantage is paramount but can be quite a *delicate* process. In essence, while the advocate screams the horrors of defendant's discrimination, he must massage the jurors' known prejudices with kid gloves.

1. Prejudice #1: "Finding Fault with the Plaintiff"

This is the most classic bias found in every civil case, but imperative to be "rooted out" in an employment discrimination trial. Sometimes referred to as the "anti-plaintiff bias," it stems from our society's belief that there are just too many frivolous lawsuits; that people are too "sensitive", and that some people will quickly sue for little or no reason. The plaintiff is thus "guilty until proven innocent" before the trial even begins.

It can sometimes be worse. A particularly defensive juror may be inclined to blame the plaintiff so as to avoid thinking that he himself might suffer a similar fate. Thus, even where a juror can identify with the Plaintiff, he may be subconsciously thinking, "This can't/won't happen to me", or "I would have complained to my supervisor much earlier if I were the plaintiff."

Trial Tactic: Find each juror's "norm" or "routine", and describe defendant's conduct as vividly inconsistent with such norms.

Jurors who are made to feel empathetic toward plaintiff are less likely to think the plaintiff could have prevented the occurrence, and more likely to recognize that someone else (defendant) may be to blame. Each juror has pre-determined thoughts of how one should act in specific situations, such as a normal and routine process. For instance, a juror who has been in a supervisory job will have a well-developed thought process about the interrelating roles of a

supervisor, employee, and top manager. During the trial, a juror is more likely to recall evidence that confirms his or her pre-existing routine process. Therefore, a goal often suggested for the plaintiff's attorney is to discover how to describe the defendant's conduct in a manner that is *inconsistent* with the juror's routine process.² The trial must make the defendant's conduct vivid so it is memorable during deliberation.

2. Prejudice #2: The Personal Responsibility Bias

The "personal responsibility" factor has become a part of popular culture in our world.³

Translated to the juror's prejudice, this "matter of choice" can be a problem for the plaintiff in a discrimination case. "If only the plaintiff had acted responsibly, he would not have to be asking for a handout from someone who has been virtuous in supplying him with a job and supporting his needs." "Why didn't he/she just leave and go somewhere else?" In other words, is plaintiff/employee unjustly trying to take advantage of others who have achieved success through hard work? After all, people should get only what they deserve.

Trial Tactic: Shift the idea of Responsibility

Confronting this attitude and making it work to the plaintiff's advantage during case preparation can restore the plaintiff's moral authority in the eyes of the jury. By making personal responsibility the central theme and using it against the defendants, moral high ground can be recovered.

The goal is to show that plaintiff is being personally responsible in family, work, community, and even in the wake of adversity at his employment. Concentrate on the strength and character of the client. Characterize the plaintiff as a fighter with a positive attitude who can and will live a productive life if given the right opportunity.

Then illustrate the defendant's irresponsibility and lack of willingness to be accountable in contrast to the plaintiff's attitude and actions.

² Id.

³ Stephen Covey, author of the best seller "*7 Habits of Highly Effective People*" claims *personal responsibility* as the foundation of this theory. Covey argues that we have the responsibility to *make things happen* and to *control* our response, a product of our conscious choice.

3. Prejudice #3: The Party with The More Limited Options Wins

In the employment setting, there is one bias which works to the plaintiff's advantage: the predisposed perception that an *employee* confronting his employer has narrow and limited options, since he does not have the controlling hand. This same bias can be made to work directly against defendant, i.e., the perception that the *employer* has many options available to address his employee's issue. Thus, the greater number of options that plaintiff presents as available to the defendant/employer, the more likely jurors will find liability.

To enhance this bias, the plaintiff's attorney should emphasize the vast availability of options, given that the employer has the total ability to change the situation according to its wanted outcome. For instance, "if only the Defendant had done 'X' or 'Y' or 'Z', this would have changed the Plaintiff's life."

Combined with the strategy found in the previous bias, plaintiff should portray defendant's conduct as unusual and different from the norm, but then reframe defendant's conduct as an action that was controllable and clear. The jury should then see that the injury was a result of the defendant clearly and controllably making a bad choice - of which plaintiff - despite his exhaustive measures to correct it - became the victim.

For the employment discrimination case, strategies to combat juror bias must remain in full force long after voir dire is ended. While there are no stock strategies that will work for each case, many common themes can be learned and perfected. Voir dire should be perceived as an opportunity to learn of a juror's specific experiences and the *impact* each had on him or her. Eliminate as much bias as possible before you seat your jury, but know that your primary challenge is to manage those prejudices once your jury is seated. Use the biases to perfect your case plan and client's story, and you are well on your way.

IV. CONCLUSION

A Plaintiff's attorney's greatest challenge is to present the client's story in a compelling, and compassionate manner, considering all the inherent prejudices and expectations of the jury. Such story, however, must be created by a strategic plan using sound legal objectives, or all the compassion in the world will not yield a verdict.



**LITIGATION TACTICS:
THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE**

FROM THE DEFENDANT'S PERSPECTIVE

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SECTION C(b)



**LITIGATION TACTICS: THE NUTS AND BOLTS OF PRACTICING AN
EMPLOYMENT LAW CASE**

From The Defendant's Perspective

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**LITIGATION TACTICS:
THE NUTS & BOLTS OF PRACTICING AN EMPLOYMENT LAW CASE
FROM THE DEFENDANT'S PERSPECTIVE**

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Overview: Seek to win at your earliest opportunity. Employment litigation from a defendant's perspective is about prevention, summary judgment and settlement. While case preparation and even legal advice centers around presenting a case before a jury, few cases are tried to a jury verdict. Most are either dismissed on a pre-trial motion or settled through the efforts of counsel or with the assistance of a mediator. The cases tried to a defense verdict will still be analyzed by most clients in terms of whether the litigation could have been avoided in the first instance. Prudent counsel, therefore, prepares his or her clients before the litigation has been initiated to help the client avoid the risk that is ever present for employers—an adverse verdict.

The earliest opportunity to win litigation is before it is filed. Fortunately, the same practices that avoid litigation are the same ones that win litigation. One of the special qualities of employment litigation is the counselor's ability to prepare the "troops" to avoid the legal battle.

I. LITIGATION TACTICS 101: WINNING WITH EARLY INTERVENTION.

Why is employment litigation filed? It is sometimes more than a legal violation. Understanding why employment litigation results is the first step to avoiding it. A lawsuit may be filed for a number of reasons unrelated to a legal violation. The formula for employment litigation is as follows:

Employee motivated to sue + actual or perceived illegality/unfairness + attorney motivated to sue = Employment Litigation.

Because the flame of employment litigation is usually the spark of three distinct elements, the defense counsel is well-advised to focus on not only legalities, but also reducing the risks of motivating an employee to sue by communicating well, reducing the risks of motivating an attorney to take the case by proper documentation, and reducing the perception of unfairness to avoid an employee's need to find counsel.

Prepare your managers/witnesses to document properly to avoid/win litigation. There are few litigators who can prepare their witnesses in advance of litigation to avoid it. Front-line supervisors and managers are, however, the future witnesses of defense counsel. They

should be trained to document well. Excellent documentation that clearly communicates and focuses on performance will deter many plaintiff's attorneys from pursuing litigation. Poorly documenting, however, is often worse than no documents at all and may be the very reason for litigation.

Documentation should focus on the facts of the situation and not the opinions of the manager writing it. It should clearly state the performance or conduct that is expected. If possible, the manager and the documentation should work on possible solutions to the performance issues provided those solutions are directed at the work and not the employee's personal affairs. Finally, the documentation should state the consequences of the future failure to abide by the rules or performance requirements.

An employer should train its supervisors to provide clear, factually-based, documentation for inadequate performance. The amount or level of documentation should stay consistent and should only focus on the performance issue at hand.

Effective documentation not only provides solid evidence of the basis for the discharge decision, it also discourages an employee from seeking legal representation and discourages an attorney from bringing suit. A well-written disciplinary memorandum may become the only reason a suit is not brought. It is the employer's opportunity to communicate with Plaintiff's counsel before the suit is filed.

A sample form disciplinary notice is attached as Appendix A.

The winning jury theme. The end of employment litigation is presenting the employer's case before a jury. So what is it that a jury wants from an employer in litigation? The answer to this question will help the employer organize its employee relations and its approach to individual employees. Defense counsel should instruct their clients on these themes so they may be used in an employer's decision-making process.

At least one jury consultant who studied employment litigation and effective themes to win employment cases before a jury, argues that an employer must focus on providing every employee a "safe" workplace. But "safety" is defined more broadly here than simply avoiding workplace injuries. "Safety" in the sense jury consultants mean it is freedom from both physical and psychological harm.

An employer should constantly and consistently seek to provide a workplace that is safe in the sense that it is fair, in the sense that employees understand what is expected of them, in the sense that the rules are evenly applied but employees are given individual treatment. This does not mean that an employee is not subject to termination or that discipline does not take place. Instead, it means that management decisions have reasons and that employees will not be subjected to random or inexplicable exercises of authority.

Have simple, well-written policies. Employment policies should be clear and concise and written to be read and understood by the average employee. Every employee handbook should have a statement that employment is at-will unless there is written employment agreement. In addition, every employee handbook should have a policy against discrimination and harassment that defines clear reporting channels and opportunity to report around the alleged harasser.

Policies should be reviewed carefully to avoid promises to an employee that an employer may not keep. For example, a promise that "Employees will be reviewed twice annually" should only be made if it is true. If an employer sometimes misses employee reviews because of the press of the business this policy may be rewritten to state, "Every effort will be made to review employees twice annually. If your review is late, you may request it at the appropriate time."

Like a well-written disciplinary memorandum, a well-written and well-conceived handbook may be an employer's first (and last) communication with plaintiff's counsel. It will then serve the dual role of communicating with the company employees and educating a potential plaintiff's counsel on the professionalism of the organization.

Be honest concerning shortcomings/avoid a hidden agenda. Employment litigation may be avoided by maintaining open, honest and clear communication with employees concerning matters pertaining to an employee's performance.

Many employers face difficulties today and tomorrow when they refuse to directly address the real reasons for employee termination or adverse employment actions and instead try to force the employee to resign. The basis for most claims of discrimination is that an employer had a hidden discriminatory reason for a discharge and the stated reason was merely a pretext. Often employers will find that they have a hidden non-discriminatory reason for a discharge but didn't have the courage to address it directly with the employee. This hidden agenda will suggest that the employer has something to hide which, in the employee's eyes, will suggest illegal discriminatory animus—a violation of the law. Notwithstanding the law, it is better to be honest and direct than to save an employee's feelings and hide the real reasons for employment actions. To work from a hidden agenda may suggest that an employer is hiding not a legal reason for its actions, but instead, an illegal reason.

Persuade your employer/clients to give an employee an opportunity to tell his or her story. Employer's should be trained that, if possible, they should allow an employee to tell his or her side of an event before termination. It may seem absurd or a waste of time, but be assured that a decision will seem unfair unless an employee is given a chance to explain him or herself. This form of "due process" is not required in employment law but it is still well-advised in all but rare occasions.

Encourage your employer/clients to follow standard procedures and use routines.

Normally evidence requires personal knowledge or recollection of the witness. What happens if you interview 300 applicants and have no recollection of the interview with an employee claiming discrimination in your interview?

Rule 406 of the Federal Rules of Evidence provides that evidence of a routine or practice is relevant to prove conduct in conformity with the routine or practice. So if you have a standard or routine in interviewing you would be able to testify to that standard or routine. In the end, the use of a standard routine or procedure in repetitive human resources actions such as interviewing not only presents the organization in a professional light but also provides the organization a vehicle to defend itself in litigation. Why shouldn't your front-line managers and human resources representatives be armed with this information before the litigation is filed? It might provide an additional reason for them to use this prudent business practice.

Periodically train supervisors/ periodically certify compliance with key policies.

The United States Supreme Court has declared that good faith efforts on the part of an employer to train its employees may be used as an affirmative defense to a claim of punitive damages in employment litigation. *Kolstad v. American Dental Ass.*, 527 U.S. 526 (1999). Training not only provides a defense, but also communicates why a particular program is important and why management wants the employees to understand the policy.

Many employers will train employees on the company's sexual harassment policy, on the warning signs of workplace violence, on effective and legal interviewing and a myriad of other topics. Likewise, supervisor training on effective documentation and compliance with employment laws is another excellent investment of an employer's resources.

As an additional defense to litigation and an additional compliance step, some employers are now requiring periodic certification by employees that the employee has complied with important policies such as the harassment policy or other ethics policies. These written certifications will provide proof of the reasonable steps an employer is making to comply with its legal obligations.

Train your clients to know when to ask for help. According to a jury verdict reporting publication, the median award in 1997 for wrongful termination/discrimination lawsuits was \$162,500 with the probability range from \$50,000 to \$407,689. These numbers will be less for Kentucky since these averages include venues that traditionally return higher verdicts. Nevertheless, the point is well made that employment litigation is expensive. Even successfully defending employment litigation is expensive.

Clients, therefore, are well-advised to seek out expert advice. It is often an excellent investment of time and/or money if faced with a tricky human resources issue or matter. Some litigation cannot be avoided but the organization's position may be strengthened with early intervention.

Attached as Appendix B is a discharge checklist that counsel may use in assisting clients with a termination decision.

II. LITIGATION TACTICS 201: WORKING TO SUMMARY JUDGMENT/AVOIDING COSTLY MISTAKES.

The complaint is filed. Now what? There are a series of issues to face immediately upon the filing of employment litigation. Failure to address any of these issues may jeopardize the chances of the case presenting for summary judgment or increase the risk and expense to the client.

Before the formal step of responding to the Complaint, defense counsel should determine, the employer's response to the allegations, the legal defenses, the witnesses, the discoverable documents, whether the case may be removed, whether there is insurance coverage and how the employer should be prepared to respond if plaintiff's counsel calls its supervisor or non-supervisory employees.

What is the employer's story? The first order of business is to determine what the employer's response is to the allegations of the Complaint. Often there has already been a demand letter by Plaintiff's counsel so this aspect of a case's development has already begun.

From the very beginning, the defense counsel should develop themes and theories that will support the story it presents. One commentator suggests that counsel capsule the case into a few sentences and use that capsule at the beginning of every court motion or response as a way to persuade the Court to your theory. For example, "This is a sexual harassment case where the employee never reported harassment until after her resignation." Another commentator suggests that counsel immediately begin to develop the opening argument to the jury from the start of the case. In either event, careful planning should be used to prepare the employer's response.

Defense counsel should also consider interviewing key witnesses at an early stage in the litigation. A firsthand rendering of the actual testimony by the live witnesses is more valuable than a secondhand delivery by a management employee involved.

Witness statements. Care should be taken to properly interview internal witnesses and to preserve attorney-client privilege. Defense counsel should consider a standard set of introductory statements to witnesses interviewed and should have a company representative present during the interview. For example, you might state,

My name is Tom Williams. I am an attorney with Ogden Newell & Welch and represent the company in litigation that has been filed by employee X. Your name has been raised by employee X as a potential witness and I want to interview you for purposes of the defense. You have the right to talk with me or not to talk to me. Whether you talk to me or refuse to talk with me will have nothing to do with

your employment. You will be neither rewarded nor penalized; your participation is voluntary. Do you understand your rights? Do you wish to speak further?

This sort of introduction will help avoid claims that you pressured an employee or that the employee was under some other form of undue influence.

In addition, a witness should be given an opportunity to read and make changes to any witness statement. Instead of reprinting these changes, it is better to simply allow the witness to write in the changes. This demonstrates that the witness was given the opportunity to correct the written statement and that makes it easier to assume the remaining parts of the statement are truly reflective of the witnesses own words.

What are the legal defenses? Defense counsel are presented with a number of legal defenses in almost every piece of employment litigation. Employment litigation touches upon discrimination law, benefits law, bankruptcy law, contract law, administrative law and any federal, state or local law that touches an employee. Defense counsel may win a case on grounds of preemption, exemptions, failure to exhaust administrative remedies or a host of other technical employment-related law that are too numerous to list.

The time to learn about these defenses is before a responsive pleading has been filed. Accordingly, every case deserves its own legal research to determine if there are new or additional defenses not previously available. Defense counsel, likewise, should be keenly aware of avoiding the waiver of a defense by failing to plead it in the answer or the first responsive pleading. See CR 12.08.

Who are the witnesses? What are the discoverable documents? How are they secured? One sure way to lose employment litigation is to destroy documents, alienate witnesses or tamper with evidence. Early preparation of the client can avoid these disasters.

Like other states, Kentucky recognizes that a court may address spoliation of evidence with a wide variety of remedies ranging from a jury instruction to dismissal of a claim or defense. Any potentially relevant documents or computer files should be preserved throughout the course of the litigation. No documents or evidence that may even remotely touch upon the litigation should be destroyed without consultation with counsel. This prohibition includes electronic mail and electronic documents.

In addition, defense counsel should be notified before an employer terminates any witness to pending litigation. The testimony of that witness may be preserved through a transcribed interview or a witness statement. Employees who have been discharged may not be willing to cooperate.

Is there insurance coverage? Defense counsel are well-advised to review any and all sources of insurance coverage with his or her client at the earliest indication that there may be

employment litigation. Even sophisticated clients may not be sufficiently aware of their existing coverage without a complete review of existing policies. Failure to timely notify the carrier of coverage may result, in some circumstances, with the denial or loss of coverage.

Is there grounds to remove the case to federal court? One of the most important defense moves in employment litigation in Kentucky is the defendant's step of removing the case to federal court if there is a federal question or diversity jurisdiction.

The summary judgment standard in federal courts is expressly more conducive to the award of summary judgment for the employer. In addition, federal judges are often more familiar with some of the complex defenses presented by employers than state judges and, on the whole, otherwise more sympathetic to the notion of dismissing employment cases.

Attached as Appendix C is a sample notice of removal based upon diversity jurisdiction.

Are the employees/management prepared for a call from plaintiff's attorney? Management employees or employees who can bind the organization with their word cannot be contacted directly by the plaintiff's counsel during litigation or upon learning that the company is being represented.

Every employer is well-advised to have a coordinated strategy and approach in handling communications by the plaintiff or the plaintiff's counsel. For management employees and employees that can bind the organization, the answer is simple: contact our counsel. For employees who may be contacted by Plaintiff's counsel, it is not improper to tell the employee that they have no obligation to speak with Plaintiff's counsel and that the employer would like to have its lawyer present when the employee speaks. Most employees want to stay out of the middle of the dispute.

The defendant's response to the complaint. Many employment claims are brought by inexperienced employment practitioners who are not sufficiently familiar with the elements of their claims. The temptation for defense counsel in these situations is to file a motion to dismiss under CR 12 or a motion for summary judgment under CR 56 right out of the gate. While in some cases this approach is warranted, in many cases the defense counsel should resist the temptation to move too quickly. A premature motion to dismiss may simply give a plaintiff and his counsel an opportunity to educate themselves to shape facts that support a viable claim. For example, an African-American employee who is discharged brings litigation for "negligence" in conducting an investigation that led to the employee's discharge and for "defamation" in reviewing his case with other members of management. Arguably, this plaintiff has not pled a cause of action under Kentucky law. Still, a motion to dismiss would likely result in the claims being recast as a race discrimination claim that might be viable.

Instead of educating plaintiff's counsel and his client on the weaknesses of their claims, the defense counsel should prepare himself as completely as possible to have his opportunity for

direct contact with the Plaintiff through the deposition. Before the deposition, defense counsel should completely review the files, the applicable policies, the necessary company witnesses and should obtain certain background information from the Plaintiff without asking the key questions.

Written discovery before the plaintiff's deposition. As indicated, defense counsel should generally work toward that immediate, unfiltered access to the Plaintiff that comes in the form of a deposition. To make that contact more meaningful, it is wise to find out certain background information before the deposition through interrogatories and document requests. Defense counsel should avoid asking the ultimate questions through written discovery and should reserve those questions to the plaintiff during the deposition. So, for example, the defense counsel should not ask in interrogatories each way in which the plaintiff claims she was discriminated because this will simply educate the plaintiff's counsel and give the plaintiff an inordinate amount of time to craft the perfect answer. Instead, the written discovery of plaintiff before the deposition should focus on background information such as previous employment, previous medical treatment, or previous involvement in criminal, civil or administrative proceedings. Armed with this information, the defense counsel will be prepared to take the plaintiff's deposition.

The plaintiff's deposition. The primary uses of the plaintiff's deposition are to secure admissions that will narrow the issues, set up inconsistencies for impeachment and establish facts that ultimately support defendant's motion for summary judgment. Certain key questions should be written in advance of the deposition so they will be asked accurately during the deposition. Defense counsel should list the elements of plaintiff's case and the employer's defenses before the deposition and direct questions to defeat the prima facie case and support the defenses.

Demeanor and approach to use during a deposition will depend upon the witness. My preference is to be cordial or neutral during the questioning unless the witness is obstructing the examination or refusing to answer straightforward questions. The examiner should maintain control of the deposition and obtain the information he or she requires. Keeping focused on the information required helps one to maintain control of the deposition. Several attempts to secure the information by your own means should be used before any resort to seeking the assistance of the court is taken.

Typically, the defense counsel must resist the temptation to "overask" key questions by continuing to probe even when the plaintiff has provided an answer that supports the defendant's position. Valuable admissions may be secured without the plaintiff realizing they are admissions that hurt his or her case.

Additionally, defense counsel must use judgment in determining whether to lead the witness with documents and other information that support summary judgment or use the same information for impeachment purposes to present at trial. For example, an e-mail may contain an admission of a critical meeting and the discussions of the meeting that the plaintiff does not

recall exists. Do you provide the e-mail to the witness early on so the testimony is consistent with the e-mail or do you hold back the e-mail and allow the witness the opportunity to speak inconsistently with what was stated in the e-mail? The answer will depend upon the objectives of the deposition and whether your client's interests are better served with consistent or inconsistent testimony.

The Motion and Memorandum for Summary Judgment. Once the plaintiff's deposition is in hand, the defense counsel may prepare the motion for summary judgment. All of the tools of effective advocacy should be used including brevity and clarity. I prefer to capsule the entire case in an opening paragraph to give the court a roadmap of the argument. Then, I will provide background facts to show the court that the result we want reached is not inconsistent with what is "just" or "right." Next, I will provide a list of "material facts" that are undisputed or undisputable. The material facts should be few and should be clearly stated. The "Argument" section will contain headings of the major points with exposition of important statutes and cases. The "Conclusion" will summarize the arguments and state the requested relief.

III. LITIGATION TACTICS 301: EVALUATING SETTLEMENT OPPORTUNITIES.

Assess the case. Winning employment litigation is really about meeting your client's realistic objectives. The realistic objectives will depend upon the strength of the employer's legal position, the perception of fairness of the decision made, the clarity of the written documentation, the number and credibility of potential witnesses, the credibility of the plaintiff and the experience and reputation of his or her counsel. Any number of these factors can and will change during the course of litigation, but a surprising number of cases can be accurately assessed early on even before any documents have been exchanged or witnesses examined.

Moreover, a surprising number of cases can be evaluated early for the likelihood that summary judgment will be granted. If the client faces a jury trial on a given case, an early assessment of settlement is warranted.

Define your objectives. Some employers will fight every litigation through to a dismissal or jury verdict. Like a government who will not negotiate with terrorists, these employers send a clear message that litigating with them will be time-consuming and costly. Other employers seek early settlement of employment litigation as an insurance policy against: (1) future litigation expenses, (2) a large judgment, (3) lost employee time in litigation, and (4) a potential public relations fall-out for losing.

Most employers will fall somewhere between the two extremes of fighting everything and settling everything. In any event, it is appropriate to have a litigation budget and an understanding of what time and expense this litigation will cause versus the potential cost to conclude the case with settlement. Many employers faced with an additional \$30,000 in expense for a *chance* to win a case will quickly accept paying \$10,000 to secure a confidential settlement

to *end* the litigation. Understanding these economics up front will allow the employer to meet its objectives and secure a “win” in litigation.

A Litigation Budget. Employment litigation is expensive. An employer not familiar with the process may be awakened to benefits of settlement by the presentation of a litigation budget. Any budget, of course, will be subject to events outside of the control of defense counsel. Still, a budget that presents a range of numbers for various stages in litigation will be instructive to a client and may educate the client to the benefits of early mediation or any early solicitation of a settlement demand.

Mediation. There are many alternative routes and means to settle a dispute early on before costs begin to soar. Mediation is an informal, non-binding, settlement conference conducted by a third party who is independent of the court and the parties. It is a quick and cost-effective means to learn whether a dispute is going to be resolved. Any party who seriously considers settlement should seriously consider mediation as a way to bring the matter to a close.

Offer of Judgment. CR 68(1) provides that “any time more than 10 days before the trial begins, a party defending against a claim may serve upon the adverse party an offer to allow judgment to be taken against him for the money or property, or to the effect specified in his offer, with costs then accrued.” CR 68(3) provides “[i]f the judgment finally obtained by the offerer is not more favorable than the offer, the offeree must pay the costs incurred after making the offer.” In addition, the offeree will not recover his or her attorney’s fees from the point of the offer if the judgment is not greater than the offer.

Thus, defense counsel may use an offer of judgment as a way to encourage settlement by putting the recovery of costs and attorney’s fees at risk. An offer of judgment should be reserved for special occasions when it appears the plaintiff’s counsel has overvalued his or her claims.

Attached as Appendix D is a sample offer of judgment.

Learn from litigation. Employers will usually benefit from a discussion with their counsel on lessons learned from the pending or recently concluded litigation. Management may freely discuss these lessons with their counsel under the protection of attorney-client privilege. If your client does what it can to make sure that any mistakes are not repeated, it will have surely claimed a “victory” in the pending litigation.

Note: This paper and the appendixes are not presented as legal advice.

About the presenter: Thomas M. Williams is partner in the Louisville law firm of Ogden Newell & Welch, PLLC. A graduate of the College of William and Mary and the University of Cincinnati School of Law, Mr. Williams specializes in employment litigation and litigation avoidance for employers. He is past Chairman of the Labor and Employment Section of the Louisville Bar Association and current Labor and Employee Relations Chair of the Louisville Society for Human Resources Management. In addition to being licenced to practice in Kentucky and Indiana, he is a past contract mediator for the Equal Employment Opportunity Commission and a certified Senior Professional in Human Resources Management. Mr. Williams is a frequent writer, speaker and trainer on human resources and employment law topics. For more information, please visit www.ogdenlaw.com.

APPENDIX A: DISCIPLINARY NOTICE

Employee: _____

Department: _____

Oral Warning

Written Warning

Other

1. Statement of the problem: (violation of rules, policies, standards, practices or unsatisfactory performance.)

2. Statement of the facts:

3. Prior disciplinary discussions or warnings: (oral, written, dates.)

4. Statement of objectives or company policy on this subject:

5. Solutions or corrective actions for improvement:

6. Employee comments:

Employee Signature

Date

Supervisor's Signature

Date

Written Warning Distribution: One copy to Employee, one copy to Supervisor and original copy to Personnel File.

Appendix B: Discharge Checklist

Discharge. Termination of employment is the most serious action an employer can take against an employee. The decision should be made after careful consideration and with a full analysis of the existing situation, its effect on the organization, and with a clear understanding that the decision is fair and defensible. Ask yourself these questions:

- What are the reasons for the discharge decision?
- How serious was the misconduct?
- Are there mitigating or aggravating factors?
- Who is the employee involved and what is his or her employment record?
- Is the employee a member of a union or seeking to organize a union?
- Have you reviewed the union contract or handbook for applicable policies and rules?
- What other written or unwritten company policies are implicated?
- Have you reviewed those policies again?
- Was the standard of conduct or performance at issue known and understood by the employee?
- Was the discharge decision properly documented?
- Will the discharge come as a surprise to the employee?
- Was the employee given an oral and written warning concerning the discharge issue?
- If no warnings, why is this a serious enough matter to warrant immediate dismissal?
- Is there any less serious discipline that should be considered such as a written warning or suspension?
- Is the employee in a protected classification of employee, e.g., over 40, female or a minority?
- How have similar matters been handled in the past?
- How have similar matters been handled with employees in and outside of protected classifications?
- If this matter is handled differently than another similar matter--why?

- Has this employee recently sought rights under any laws such as worker's compensation, FMLA, OSHA, harassment, wage and hour or any other federal, state or local laws?
- How important is this employee to the Company? How easy or difficult will it be to replace him or her?
- Would the decision seem fair to someone outside of the organization?
- Is there anyone else who should be part of the discharge decision review?
- Does the employee record generally support the decision e.g. performance evaluations and other employee records?
- Has the employee had an opportunity to explain himself or herself? Should the matter be investigated further?
- Does the employee have legal counsel or has the employee threatened litigation?
- Is there any other reason you are aware of that may cause the employee to legitimately challenge the decision?

Appendix C: Notice of Removal to Federal Court/Diversity

Federal Court Case Style

PLEASE TAKE NOTICE that Defendant hereby removes the above-entitled action from the Commonwealth of Kentucky Jefferson Circuit Court, to the United States District Court for the Western District of Kentucky, Louisville Division, on the basis of diversity of citizenship, pursuant to 28 U.S.C. §§ 1332 and 1441(a).

In support of the removal action, Defendant alleges as follows:

1. On or about January 30, 2002, a civil action was filed against Defendant by Plaintiff in the Commonwealth of Kentucky Jefferson Circuit Court entitled Plaintiff v. Defendant, Inc., Case No. 02CI00781 ("Action"). A true and correct copy of the original Complaint ("Complaint") filed in the Action, along with summons thereon, is attached hereto as Exhibit A and is incorporated herein by reference.

2. Defendant was served with summons and a copy of the Complaint on January 31, 2002.

3. Exhibit A constitutes all of the pleadings and paper in the Action of which Defendant is aware.

4. This action is removable pursuant to 28 U.S.C. §1441(a) and 28 U.S.C. §1332 because the citizenship of the parties is diverse and the amount in controversy exceeds the jurisdictional requirement. First, it is a civil action between citizens of different states. Plaintiff is a citizen and resident of the Commonwealth of Kentucky and is domiciled in the Commonwealth. Defendant's state of incorporation is Nevada with its principal place of business in San Antonio, Texas. Second, Plaintiff is seeking compensatory damages, including lost salary, lost employment benefits, emotional distress, humiliation and embarrassment, as well as punitive damages. Based upon

Defendant's good faith belief and the pleadings and attachments thereto, the amount in controversy exceeds the sum of \$75,000, exclusive of interest and costs. This Court has original jurisdiction over the Action under 28 U.S.C. § 1332.

5. Therefore, pursuant to 28 U.S.C. §1441(a), this Action is removable to this Court.

6. This Notice of Removal is timely filed with this Court pursuant to 28 U.S.C. §1446(b), as it is being filed within 30 days after receipt by Defendant of the initial pleading in this Action.

7. The adverse party has been given prompt written notice of removal by service of this Petition.

WHEREFORE, Defendant hereby removes the Action to this Court.

Dated: February 28, 2002.

Thomas M. Williams
Craig C. Dilger
OGDEN, NEWELL & WELCH PLLC
1700 PNC Plaza
Louisville, KY 40202
(502) 582-1601
Attorney for Defendant,

Appendix C: Notice of Removal to State Court

State Court Case Style

NOTICE OF REMOVAL TO FEDERAL DISTRICT COURT

To: Plaintiff's counsel
239 South Fifth Street, Suite 1700
Louisville, Kentucky 40202-3268
Counsel for Plaintiff

Please take Notice that Defendant in the above-entitled action, filed a Notice of Removal, a copy of which is attached hereto, on February 28, 2002, in the office of the Clerk of the United States District Court for the Western District of Kentucky, Louisville Division.

DATED: February 28, 2002.

Appendix D: Sample Offer of Judgment

Counsel
11420 Bluegrass Parkway
Louisville, Kentucky 40299

**RE: Employee v. Company; Jefferson Circuit Court, Division Eleven (11);
Civil Action No. 01CI-05565**

Dear Counsel:

As of today's date, Defendants collectively offer to allow judgment to be taken against them in the amount of \$10,000.00, inclusive of costs and fees.

This offer is governed by CR 68. Under CR 68(1), your client has ten (10) days to accept this offer. Under CR 68(3), "[a]n offer not accepted shall be deemed withdrawn and evidence thereof is not admissible except in proceedings to determine costs."

I will address discovery matters in a separate letter to follow.

Sincerely,

Thomas M. Williams



**THE EMPLOYER'S DUTY TO ACCOMMODATE
AN EMPLOYEE'S RELIGIOUS BELIEFS**

Article

*LaToi D. Mayo
Debra H. Dawahare
Wyatt, Tarrant & Combs, LLP
Lexington, Kentucky*

Slide Show Notes

*Debra H. Dawahare
Wyatt, Tarrant & Combs, LLP
Lexington, Kentucky*



**THE EMPLOYER’S DUTY TO ACCOMMODATE
AN EMPLOYEE’S RELIGIOUS BELIEFS**

PART ONE: ARTICLE D-1

I. INTRODUCTION D-1

II. WHAT IS RELIGION FOR PURPOSES OF TITLE VII D-2

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THE EMPLOYER'S DUTY TO ACCOMMODATE AN EMPLOYEE'S RELIGIOUS BELIEFS

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I. INTRODUCTION

Title VII of The Civil Rights Act of 1964 prohibits discrimination in the workplace based upon employees' sincerely held religious beliefs. In 1972 Congress amended Title VII of the Civil Rights Act of 1964 to add as a distinct obligation of employers the duty to reasonably accommodate the religious practices of employees to the extent that they can do so without undue hardship. In imposing upon employers the duty to reasonably accommodate the religious practices and observances of employees if they can do so without undue hardship, Congress did not define the terms "reasonable accommodation" or "undue hardship." Congress never amended the definition of "religion" in which such terms are used, or otherwise given substantive guidance as to the meaning of such terms since 1972.

Religious discrimination in employment has been the subject of state as well as federal legislation, and the courts have been called upon to define the circumstances under which particular circumstances have resulted in an employer's failure to reasonably accommodate the religious beliefs of the employee. As the courts have grappled with interpreting these terms in a variety of factual contexts, some general principles have emerged. Viewing the cases generally, the courts have taken seriously Congress's attempt to impose upon employers an affirmative duty to accommodate the religious practices of employees which is in addition to, and distinct from, the obligation to not discriminate against an employee on the basis of religion. However, it is also clear that if an employer makes a good faith effort to accommodate the religious practices of the employee, it will generally have no major difficulty in establishing either that it has reasonably accommodated the employee or that to do so would impose undue hardship. At a minimum, the employer must negotiate with the employee in an effort to reasonably accommodate the employee's religious beliefs and then the employee has a duty to make a good faith effort to attempt to accommodate his or her religious needs through means offered by the employer.

Acknowledging the above facts, this article will attempt to address: (a) recent cases discussing the requirements for religious accommodations; (b) the state of the law in Kentucky surrounding an employer's obligation to reasonably accommodate; and (c) religious accommodations that directly conflict with other workplace policies.

II. WHAT IS RELIGION FOR PURPOSES OF TITLE VII

Title VII defines “religion” to include all aspects of religious observance, practice, and belief.¹ 42 U.S.C. § 2000e(j). One purpose of defining “religion” so broadly is to minimize the need for judicial decisions in which particular beliefs and practices qualify as a “religion” in order to avoid the excessive entanglement of church and state prohibited by the First Amendment. On occasion, however, courts have had to decide what “religion” is. “Religion,” within the meaning of Title VII, has also been found to include: the Black Muslim faith, the “Old Catholic” religion, and atheism. “Religion,” within the meaning of Title VII, has been found to include the Wicca religion or “The Old Religion.” In *Van Koten v. Family Health Management, Inc.*,² the court held that “a religious belief does not have to be espoused by or accepted by any religious group to fall within the definition of ‘religion’ under Title VII.” Applying the *Redmond* test, the court held that Wicca may be considered a belief which is sincerely held in the plaintiff’s “own scheme of things.” But since the court found that the plaintiff had failed to satisfy the notice requirement of his prima facie case, they affirmed the lower court’s grant of summary judgment.

Courts have also been called upon to determine whether a certain practice or belief is “religious” for purposes of Title VII. Notwithstanding Title VII’s broad definition of religion, there are limitations on what constitutes a legitimate “religion” or a “religious practice or belief”. The discussion which follows will outline the general principals all courts follow in analyzing these issues.

In the landmark case of *Redmond v. GAF Corporation*³, the court set forth the proper test for determining what is a protected “religious practice or belief.” Redmond was a Jehovah’s Witness. Church elders appointed him to be in charge of a Bible study class. All went well so long as the class met on Tuesday nights. When the elders changed the meeting time to Saturday mornings, the schedule conflicted with GAF’s required Saturday overtime. Redmond claimed that even though his employer was aware that he could not work on Saturday because of his “religious obligation,” his supervisor told him that either he agreed to work or he would lose his job. When he told them he would not be able to work the scheduled overtime on the coming Saturday, he was terminated. The district court found that the discharge discriminated against the employee in exercise of his religion and the employer appealed.

The Court of Appeals held that the employee’s participation in Saturday bible class activities constituted a statutorily protected “religious obligation.” GAF argued on appeal that, because Saturday work per se was not prohibited by the plaintiff’s religion, the practices in question were outside Title VII’s. The court disagreed. It relied principally on the statute’s explicit language in support of its conclusion. “The term ‘religion’ includes **all aspects of religious observance and practice, as well**

¹ 42 U.S.C. § 2000e(j).

² *Van Koten v. Family Health Management, Inc.*, 955 F. Supp. 898 (N.D. Ill. 1997) (emphasis added).

³ *Redmond v. GAF Corporation*, 574 F.2d 897 (7th Cir. 1978).

as belief ...”⁴ The court held that these words leave little room for the limited interpretation that Title VII protection is found only in situations where either “Sabbatarianism” or a practice specifically mandated or prohibited be a tenet of the plaintiff’s religion is involved. Second, the court noted that:

...to restrict the act to those practices which are mandated or prohibited by a tenet of the religion, would involve the court in determining not only what are the tenets of a particular religion, which by itself perhaps would not be beyond the province of the court, but would frequently require the courts to decide whether a particular practice is or is not required by the tenets of the religion.⁵

The court found that such judicial determination would be “irreconcilable” with the Supreme Court’s holding in *Fowler v. Rhode Island*.⁶ “it is no business of courts to say ... what is a religious practice or activity...” The court found that the proper test to determine what is “religious” under Title VII is whether (1) the “belief” for which protection is sought religious in person’s own scheme of things, and (2) is it “sincerely held.”

The evidence established that Redmond was sincere in his religious beliefs, having been a member in his church for over 16 years. It further established that he was appointed to be a lifetime leader of the Bible study class and had done so for many years. Redmond testified that he felt his participation in the Saturday activities was at the dictate of the elders therefore a “religious obligation.” Thus, applying the above test with these facts, the court concluded that the practice in question was within Title VII’s protection.

The Sixth Circuit adopted the test set forth in *Redmond* to be applied in determining what is “religious” in *Dorr v. First Kentucky National Corp*.⁷ In this case, Dorr appealed the lower court’s dismissal of his Title VII employment discrimination suit. He alleged that actions directed against his religious activities forced him to resign from the defendant bank. Dorr was a member and president of Integrity, an organization that is affiliated with the Episcopal Church and that advocates equal rights for homosexual men and women within the church and society as a whole. Dorr claimed that after he was appointed president of a local chapter of Integrity, he was forced to resign.

The district court found that Dorr did not sincerely believe that his religion “required” him to serve as president of Integrity, and therefore those activities were not motivated by sincere religious beliefs. The court of appeals reversed. It concluded that although the district court recited the applicable standards, it erred in applying them. The court stated that the “concept of religion embraced by the statute, is not, we think, one of an external set of forces and rules that compel an individual to act one way or another... The question is not one of compulsion, but one of motivation.” Therefore,

⁴ 42 U.S.C. § 2000e(j)(emphasis added).

⁵ *Redmond* at _____.

⁶ *Fowler v. Rhode Island*, 345 U.S. 67, 70, 73 S.Ct. 526, 527 (1953).

⁷ *Dorr v. First Kentucky National Cor.*, 41 Fair Empl. Prac. Cas. (BNA) 421 (1986)

the court found that in applying the *Redmond* test, courts must not stop at a finding that one does not sincerely believe that he is required by his religion to perform a certain practice or “obligation;” they must also find whether participation or performance was **motivated by religious beliefs**. The court stated “his sincerely held religious beliefs may motivate his activity even though they do not require it.”⁸

The First Circuit recently explained the phrase “sincerely held belief” for purposes of Title VII protection in *E.E.O.C. v. Union Independiente De La Autoridad de Acueductos*.⁹ This case involved David Cruz-Carillo, a member of the Seventh-Day Adventist Church who claimed that the tenets of his religion prohibit him from joining a labor organization. Cruz alleged that the defendant mandated that he join in order to keep his job.

The union argued that the district court erred in granting summary judgment due to the fact that there remained disputed issues of fact with respect to the question of whether Cruz’s objection to union membership was the product of a “bona fide religious belief.” In support of its argument, the defendant relied on the evidence tending to show that Cruz had on several occasions taken actions that were at odds with his professed faith. The Court of Appeals agreed. It began by stating, “while the ‘truth’ of a belief is not open to question, there remains the significant question of whether it is truly held.” The court found that the element of sincerity is fundamental, since without sincerity, there can be no showing of a religious observance or practice that conflicts with an employment requirement. The court reasoned that findings on this issue will necessarily depend on the factfinder’s assessment of the employee’s credibility. These issues are fact questions and should not ordinarily be disposed of by summary judgment. The court continued that the evidence tending to show that an employee acted in a manner inconsistent with his professed religious belief is relevant to the evaluation of sincerity. The court found that there was evidence establishing that Cruz only objected to certain membership requirements and he showed opposition to any form of union membership only after the union agreed to accommodate him with respect to each practice he had identified earlier. Such evidence, the court stated, “if credited by the factfinder, could bear on the sincerity of Cruz’s belief.” The court cautioned other courts to “be careful in separating the verity and sincerity of an employee’s beliefs in order to prevent the verdict from turning on the factfinder’s own idea of what a religion should resemble.”¹⁰

Title VII does not protect an employee’s “personal preferences.” In *Vetter v. Farmland Industries, Inc.*,¹¹ Dean Vetter sued his employer, Farmland Industries, for terminating him for refusing to move to his trade territory. Vetter argued that his religious beliefs required him to live in a city with an active Jewish community and synagogue and that Farmland had discriminated against him on the basis of his religion by enforcing its residence requirement and not accommodating his beliefs. A jury

⁸ *Id* at 421.

⁹ *E.E.O.C. v. Union Independiente De La Autoridad de Acueductos*, 279 F.3d 49 (1st Cir. 2002).

¹⁰ *Id.* at 54, quoting *Philbrook v. Ansonia Bd. Of Ed.*, 757 F.2d 476, 482 (2d Cir. 1985).

¹¹ *Vetter v. Farmland Industries, Inc.*, 120 F.3d 749 (8th Cir. 1997).

returned a verdict for Farmland, but the district court granted Vetter's motion for judgment as a matter of law. Farmland appealed and the court of appeals reversed.

Farmland argued that the district court erred by overturning the jury verdict. It believed that the desire to live near others of the same religion was not an "observance or practice" that must be accommodated. The court stated that under the jury instructions Vetter had to show that he had a sincere belief that compliance with Farmland's residence requirement conflicted with his religious observance or practice and that his decision to live in Ames did not reflect a purely personal preference." Since the evidence was in conflict on this point, and the court held that it was a matter for the jury to resolve. The evidence showed that Vetter chose to live in Ames as a matter of personal preference, and not because living in the Webster City area would have conflicted with an observance or practice of his religion. Farmland witnesses testified that Vetter agreed in his interview to live in the Webster City area and living there was required. Vetter testified that he had looked for a home in the Webster City area but was unable to find rental housing. He further acknowledged that he wanted to live in Ames in part because he had found suitable housing there and the schools had a good reputation. Furthermore, the evidence showed that before Vetter accepted the job he lived in a city which did not have a synagogue and from where he commuted 45 miles to religious services. Had he moved to Webster City, he would have been approximately the same distance from a synagogue as he was previously. Thus, the court concluded "the reasonable inference that could be drawn from it was sufficient to support the jury verdict in Farmland's favor."

The federal courts have been consistently adopted and applied the *Redmond* test. Courts will not evaluate the "truth" of one's belief; however, they will allow evidence which tends to prove or disprove whether the belief is in fact sincerely held. Evidence establishing that the belief is not sincerely held leads to a possible finding that the belief is not motivated by religion, but rather by personal preference. Although case law provides the above basic principles, each case must be evaluated separately based on its own specific facts.

III. RECENT CASES DISCUSSING RELIGIOUS ACCOMMODATION

A. M. Bruff v. North Mississippi Health Services, Inc., 244 F.3d 495 (5th Cir. 2001).

The Plaintiff was employed by the defendant as a counselor in its Employee Assistance Program (EAP). Early in 1996, Bruff began counseling a woman identified only as Jane Doe. After several months, Doe informed Plaintiff of her homosexuality and asked for help in improving her relationship with her female partner. Bruff declined to counsel her on that subject, advising that homosexual behavior conflicted with her religious beliefs, but offered to continue counseling her on another matter. Doe complained to her employer, who in turned complained to the medical center. Bruff's supervising counselor arranged a meeting to explore the matter, at which Bruff was asked, per company policy, to put in writing exactly what aspect of her counseling responsibilities she wanted to be excused from. Bruff wrote a letter generally asking to be excused from providing assistance in improving homosexual or extramarital relationships. In response to this letter, management met several times to determine if plaintiff's request could be accommodated by shifting responsibility among the three EAP counselors. Eventually it was determined that accommodation would not be feasible. Management then denied Bruff's request stating that, "Our EAP contract

obligates us to treat a wide variety of psychiatric services and clinical issues" and does not exclude certain categories of issues for individuals with certain types of issues. When the possibility of transferring from EAP to a section specifically performing pastoral or Christian counseling was discussed, Bruff declined. The vice president then offered three options: (1) reconsider her request for accommodation; (2) request a transfer to another position or department in which conflicts were less likely to occur; or (3) resign her position. If she decided to request a transfer, she would be given 30 days to secure another position before she would be terminated. During this 30-day period, Bruff applied for one other position which was given to another applicant with superior credentials. Although there was another counseling position available, she did not apply and at the end of the 30-day period Bruff's employment was terminated.

The district court magistrate dismissed the state law claims on a motion for directed verdict. However, he did enter a judgment on the jury finding that the employer had violated Title VII. The jury found that the Medical Center had discriminated against Bruff because of her religious beliefs, that it had not made a reasonable accommodation for those beliefs, and that it acted with malice or reckless indifference to Bruff's sincere beliefs. The defendant appealed.

The issue in this case was to what extent Title VII required the Medical Center to accommodate Bruff's religious beliefs. The Court of Appeals held that the hospital was not required under Title VII to accommodate the plaintiff by excusing her from a counseling on a subject which conflicted with her religious beliefs, as such accommodation would have constituted an undue burden as a matter of law. The court also concluded that the hospital offered reasonable accommodations to the plaintiff as a matter of law when the hospital offered to give her 30 days to find another position at the hospital where the likelihood of encountering further conflicts with her religious beliefs would be reduced, and the court finally concluded that the plaintiff's termination was not wrongful under the Mississippi public policy exception to the employee at will doctrine.

The court began its analysis by looking at the Medical Center's motion for judgment as a matter of law. The court noted that after Bruff established her prima facie case of religious discrimination under Title VII, the burden shifts to the employer to show why accommodating her religious beliefs as requested would cause them an undue hardship or that they have offered a reasonable alternative accommodation to resolve the conflict. The court stated that accommodation can take place in two ways: (1) an employee can be accommodated by his/her current position by changing the working condition or (2) the employer can offer to let the employee transfer to another reasonably comparable position where conflicts are less likely to arise.

In relation to the first method of accommodation, the Medical Center argued that retaining Bruff in her position would cause an undue hardship, relying on the Supreme Court's holding in TransWorld Airlines v. Hardison, 432 U.S. 63, 97 S.Ct. 2264, 53 L.Ed.2d 113 (1977), holding that an undue hardship exists as a matter of law when an employer incurs anything more than a minimal cost to reasonably accommodate an employee's religious beliefs. Bruff determined that she would not perform some aspects of the position itself. The court found this to be an inflexible position. Relying on Weber v. Roadway Express, 199 F.3d 370 (5th Cir. 2000), the court stated that Title VII does not require an employer to accommodate inflexible religious accommodations affecting other employees. The Defendant contended, and the court found the record supported, that given the size

of the EAP staff, the area covered by the program and travel involved, and the nature of psychological counseling incorporating trust relationships developed over time, any accommodation of Bruff in an EAP counseling position would involve more than a minimal cost to the Medical Center. The court found that requiring one or both counselors to assume a disproportionate workload, or to travel involuntarily with Bruff to sessions to be available on a case by case basis in case a problematic subject matter came up, is an undue hardship as a matter of law.

In relation to the second way to accommodate by transferring an employee to another counseling position, the court found that Title VII does not restrict an employer to only those means of accommodation that are preferred by the employee. Thus, once the medical center established that it offered Bruff a reasonable accommodation even if not her preference they have, as a matter of law, set aside their obligations under Title VII. The court rejected the plaintiff's reliance on ADA claims handling reasonable accommodations and undue hardship, stating that there was a distinction in the definition of reasonable accommodation and undue hardship from ADA claims and Title VII claims. The court found that when the medical center gave her 30 days to find another position, it also alerted in-house counsel to the situation and directed that Bruff be given assistance in finding other employment at the medical center. The court concluded that an employee has the duty to cooperate in achieving accommodations of his/her religious beliefs and thus be flexible in achieving that end. The court found that Bruff displayed almost no such cooperation or flexibility in that she refused to be tested for other positions, declined to even consider a pastoral position, and refused to even apply for a second counseling position.

B. Ali v. Alamo Rent-a-Car, 8 Fed. Appox. 156 (4th Cir. 2001).

An Islamic employee brought action against her employer under Title VII for refusing to allow her to wear a head scarf at work that was mandated by her religion. Alamo hired Ali as a management trainee. While on the job, she wore a head scarf along with her company uniform. A new supervisor told Ali that she would have stop wearing the head scarf or be transferred to a position in which she would not be in frequent contact with customers. Ali refused to stop wearing the scarf and thereafter she was transferred. After the transfer, Ali filed suit. The district court granted the employer's motion to dismiss for failure to allege an adverse employment action. The court gave her 11 days to amend the complaint alleging such action. Plaintiff concluded that she would not meet the standard, therefore she filed a motion to amend arguing that Title VII religious discrimination did not require such adverse employment action. The trial court denied the employee's motion to amend its judgment. The employee appealed and the Court of Appeals found that the employee was required to allege adverse employment action to survive the employer's motion to dismiss for failure to state a claim.

The issue in this case was whether Title VII religious discrimination claims require a showing of adverse employment action. Ali claimed that the accommodation provision in the statutory definition of "religion" dictates that religion should be treated differently, unlike other bases for discrimination, religion does not require a showing of adverse employment.

The court began its analysis by setting forth the definition of religion. "Religion" is defined as including "all aspects of religious observance and practice, as well as belief, unless an employer

demonstrates that he is unable to reasonably accommodate an employee...religious observance or practice without undue hardship in the conduct of the employer's business." 42 U.S.C. § 2000(e)(j). The court noted that Congress inserted this provision in the definition in the wake of Dewey v. Reynolds Metal Company, 429 F.2d 324, 330 (6th Cir. 1970), affirmed by an equally divided court at 402 U.S. 689, 91 S.Ct. 2186, 29 L.Ed.2d 276 (1971). In Dewey, the circuit court held that an employer does not discriminate on the basis of religion simply by failing to accommodate employees' religious practices. The court concluded in light of Dewey the accommodation provision is a clarification that an employer does discriminate on the basis of religion if it cannot accommodate a religious practice without undue hardship. However, relying on the explicit language in the statute, the court concluded that the accommodation provision does not affect the underlying requirement that the employer's discriminatory practice relate to "compensation, terms, conditions or privileges of employment" or that the practice "deprives any individual or employment opportunity or otherwise adversely affect the status of an employee." 42 U.S.C. § 2000(e). Therefore, the court found that Ali's reliance upon the accommodation provision in the definition of religion was misplaced.

Ali also relied upon the legislative history accompanying the adoption of the accommodation provision to support her argument that religious discrimination claims do not require a showing of adverse employment action. Ali cited the history in which Congress expressed concern with the Dewey decision. However, the court concluded that Congress' concern about said decision was not inconsistent with Title VII's requirement for adverse employment action. Likewise, the court rejected Ali's reliance on the EEOC regulations implementing Title VII with respect to religious accommodations. The court concluded that the regulations merely track the language of the statute and do not address the issues in this case. Finally, the court rejected Ali's claim that case law supported her argument stating that "none of the cases she cites stand for, or even suggest, such a proposition."

IV. THE "RELIGIOUS INSTITUTION" EXEMPTION

Hall v. Memorial Health Care Corp., 215 F.3d 618 (6th Cir. 2000).

A terminated college employee brought a religious discrimination claim under Title VII. The District Court for the Western District of Tennessee entered summary judgment for the college. The employee appealed. The Court of Appeals held that (1) the college of health sciences qualified as a religious educational institution entitled to Title VII exemption from religious discrimination claims based on this direct relationship with the Baptist church; (2) the religious exemption was not waivable, and (3) the employee did not state a prima facie case of religious discrimination and the college's proffered nondiscriminatory reason was not pretextual.

Plaintiff Glynda L. Hall sued her former employer, Baptist Memorial College of Health Sciences, alleging that the College unlawfully terminated her employment based on her religion. The Baptist Memorial Health Care Corporation (Corporation) is a non-profit corporation established with the purpose of "carrying out a health care mission consistent with the traditional and ongoing health care missions of the Arkansas, Mississippi and Tennessee Baptist Conventions and their affiliates." The Corporation is the parent of Baptist Memorial Hospital which, in turn, is the parent

of Baptist Memorial College of Health Sciences. The Hospital's charter states that it is a non-profit corporation organized for "charitable, educational, religious and scientific" purposes and that its purposes include "hospital and health care and education ... in line with the traditional and ongoing mission of the Baptist churches affiliated through their State Baptist Conventions in Arkansas, Mississippi and Tennessee with the Southern Baptist Convention as now known and practiced among Baptists." Id.

On August 7, 1995, the College hired the plaintiff as a Student Services Specialist. In that position, Hall worked with students and the administration in organizing and planning activities of various campus student organizations. Hall was responsible for interpreting school policies and ensuring that all student activities were consistent with the mission of the College. Hall was later ordained as a minister at Holy Trinity, a church which teaches that there is nothing inherently inconsistent between the homosexual lifestyle and Christianity. The Southern Baptist Convention is outspoken against homosexual lifestyles. Hall's position at the College was perceived as being one of considerable influence over students and since the Holy Trinity's views on homosexuality were inconsistent with those of the College, Hall was asked to resign. The College did offer to help her obtain another position at the College for which she was qualified. Hall refused and the College terminated her for a "conflict of interest." Id.

Hall raised three issues on appeal: (1) whether the district court erred in finding that the College was a religious institution entitled to an exemption from Title VII's prohibition against religious discrimination; (2) whether the district court erred in finding that the statutory Title VII exemption was not waivable; and (3) whether the district court erred in finding that Hall did not state a prima facie case of religious discrimination, and in finding that the College's proffered nondiscriminatory reason was not pretextual.

The court began its analysis by recognizing that Title VII has expressly exempted religious organizations from the prohibition against discrimination on the basis of religion. The court stated that "the decision to employ individuals of a particular religion has been interpreted to include the decision to terminate an employee whose conduct or religious beliefs are inconsistent with those of its employer." See, Little v. Wuerl, 929 F.2d 944, 951 (3rd Cir. 1991). The court reasoned that the College qualifies for the exemption under the plain language of § 2000e-2(e)(2) because it is a "school, college, university, or other education institution or institution of learning ... that ... is, in whole, or in substantial part, owned, supported, controlled, or managed by a ... religious corporation." The court further found that the College was founded by three sectarian organizations and that the atmosphere was permeated with religious overtones.

Additionally, the court rejected Hall's contention that even if the College was a religious educational institution, it waived the Title VII exemption for such institutions because it represented itself as being an equal opportunity employer and because it received federal funds. Relying on previous decisions addressing this issue, the court found that the statutory exemptions from religious discrimination claims under Title VII could not be waived. See, Little, supra; Siegal v. Truett-McConnell College, Inc., 13 F. Supp.2d 1335 (N.D. Ga. 1994).

Finally, Hall argued that the district court erred in finding that she failed to establish her prima facie case or that she failed to prove that the College's articulated reason for firing her was pretextual. Under this analysis, the court focused on whether Hall had shown that she was treated less favorably than similarly-situated persons not a member of the protected class. The court relied heavily on the district court's finding and held that Hall failed to establish that "a similarly-situated co-worker received more favorable treatment than she." The court found that an ordained minister in the Methodist Church and two employees who were committing an adulterous relationship were not similarly situated co-workers in that neither assumed a leadership position in an organization that publicly supported homosexual lifestyles. Similarly, the court found that Hall failed to show that the reason for her termination was a pretext for discrimination based on her religion. The court stated that "to show that termination was based on her religion, Hall must show that it was the religious aspect of her leadership position that motivated her employer's actions. Id. at 626.

In this case, the employee tried to analyze this case as a reasonable accommodation claim, arguing that the employer must reasonably accommodate her religious beliefs. The court rejected the employee's reasonable accommodation claim stating,

In reasonable accommodation religious discrimination cases, a plaintiff must establish that it holds a sincere religious belief that conflicts with an employment requirement, that it inform the employer of the conflict, and that it was discharged or dismissed for failure to comply with the conflicting requirement.

The court stated that this analysis was not relevant to this case since Hall's employers did not direct her to do anything that conflicted with her religious beliefs, and Hall was not terminated over a failure to perform any duties which conflicted with her religious beliefs. It further found, "even if this case could be so characterized, the evidence shows that the college president had a list of available positions she offered to help Hall obtain if Hall would have agreed to resign her position as a student services specialist. Hall declined this reasonable accommodation and was terminated." Id.

V. THE STATE OF LAW OF RELIGIOUS ACCOMMODATION IN KENTUCKY

A. State Cases

Kentucky Revised Statute § 344.040 prohibits religious discrimination in employment and requires employers to make reasonable accommodations to the religious needs of employees. The discussion that follows briefly summarizes the state of the law on religious accommodations in Kentucky in relation to Title VII.

In Human Rights v. Commonwealth, Department for Human Resources, Hazlewood Hospital, 564 S.W.2d 38 (Ky. App. 1978), the court decided that a hospital's effort at accommodating a nurse aide trainee's religious belief was inadequate to satisfy the rule of reasonable accommodation for purposes of Kentucky Revised Statute § 344.030(5) and 344.040. The record revealed that the nurse's aid trainee was a member of the Worldwide Church of God, which required that members in good standing abstain from gainful employment from sunset Friday to sunset

Saturday and on seven (7) holy days. After accepting a job at the hospital, she informed the nursing supervisor that she could not work on these days, but she offered to work on other days, including Sunday. The supervisor informed her that no accommodation could be made for her religious observance, and she was reported as having declined the position for refusal to work the scheduled hours. The record showed, however, that the hospital later offered her an open exam booklet that listed classifications currently being tested by the Commonwealth.

The court stated that the U.S. Supreme Court's interpretation of federal statutes and regulations as set forth in TransWorld Airlines v. Hardison 432 U.S. 63, 97 S.Ct. 2264, 53 L.Ed.2d 113 (1977) was persuasive, if not controlling, in interpreting the similar requirements of state law, namely that employers must make reasonable accommodations to the religious needs of present and prospective employees where such accommodation can be made without undue hardship. In the court's view, the standard for demonstrating undue hardship had shifted from a "dire effect" standard to a new rule, set forth in the TransWorld Airlines case, that more than a "de minimus cost" in the form of either loss efficiency or premium wages would constitute undue hardship. The court observed that even though the nurse aide trainee had made a genuine attempt at a solution by offering to work any days other than her Sabbath and special religious holidays, the employer had offered only to try and find a position other than that of nurse aide for which she applied. The court concluded that the employer's efforts were not reasonable attempts at accommodation, since an additional effort to investigate the possibility of swapping time with other employees could have been made without causing undue hardship.

Likewise, in Kentucky Commonwealth on Human Rights v. Kerns Bakery, Inc., 644 S.W.2d 350 (Ky. App. 1982), the court found that a bakery illegally discriminated against an oven operator who did not work on his Sabbath because it did not comply with the reasonable accommodation provisions of Kentucky Revised Statute § 344.030(5) which provides that otherwise unlawful discrimination because of religion was lawful if the employer demonstrated an inability to reasonably accommodate employees' religious observance or practice without undue hardship.

The case involved a roll oven operator who became a member of the East Eighty Free Pentecostal Holiness Church. When he advised the supervisor of his religious belief against Sunday work and sought accommodation by way of a transfer to an available non-Sunday job or by being excused from Sunday work, the bakery made no effort to accommodate him and when he failed to report for work for three Sundays, he was fired. The court approved the state Human Rights Commission's findings that the bakery had failed a statutorily required duty of making efforts to reasonably accommodate the oven operator's religiously based refusal to work on Sunday, and its findings that the bakery could have easily accommodated the oven operator without undue hardship to its business by either transferring him to an available non-Sunday job or simply excusing him from Sunday work. The court therefore reversed the trial court's judgment dismissing the complaint on constitutional grounds and reinstating the state Human Rights Commission's order finding a violation of the state anti-discrimination law.

However, a tire company did not violate the Kentucky Civil Rights Act, Kentucky Revised Statute § 344.040, which outlawed discharge because of religion, when it fired a lab technician for refusal to work on his Sabbath, because the company's efforts to accommodate the lab technician

were found to be reasonable. Evans v. General Tire & Rubber Co., Mayfield Division, 662 S.W.2d 843 (Ky. App. 1983). The company's lab employees, who were not unionized, were required to work occasional overtime during the week and on Saturdays, and they worked out a voluntary rotational system to equalize the number of Saturdays worked by each, subject to individual trade-offs to accommodate conflicts of a personal nature. The lab technician then became a member of the Worldwide Church of God, whose Sabbath extended from sundown Friday to sundown on Saturday, and based on his religious beliefs he advised his supervisor that he would no longer work any Saturdays. He was successful in getting voluntary replacements for about five months, but when he could not get a replacement and refused to work on four Saturdays, he was fired. The court noted that § 344.040 outlawed discharge because of religion unless the employer cannot reasonably accommodate an employee's religious observance or practice without undue hardship. The court disapproved the findings of the state Commission on Human Rights in this case, which found that the company could have reasonably accommodated the lab technician's need not to work on Saturdays without undue hardship, saying that the state's Commission wrongfully believed that undue hardship could only result legally where there is a collective bargaining agreement or contractual right to shift a job preference. Rather, said the court, undue hardship could also result if accommodation would lead to preferential treatment of some employees on the basis of religion. The court found that all the lab technician's fellow employees obviously objected, as the lab technician could find no one to substitute for him on the Saturdays in question, and it pointed to undisputed testimony of morale problems on account of attempts to accommodate the lab technician's religious practices. The loss of efficiency and the resulting cost to the company as a result of forcing others to work for the lab technician on Saturdays, continued the court, would obviously be more than de minimus. Accordingly, the court affirmed the trial court's order setting aside the state Commission's findings of religious discrimination by the company.

The Sixth Circuit, in the following cases, has held that under the circumstances presented, that proposed accommodation of the employee's religious practice imposes an undue hardship on the employer for purposes of the Civil Rights Act of 1964.

The court in Reed v. Memphis Publishing Co., 521 F.2d 512 (6th Cir. 1975) held that the employment of a copy reader who refused to work Saturdays for religious reasons would have caused undue hardship to the employer for purposes of regulations issued by the Equal Employment Opportunity Commission pursuant to Title VII of the Civil Rights Act of 1964 because (1) it would require the employer to assign involuntarily other employees to take the employee's place on Saturdays, resulting in a daily overtime expense of \$77; (2) the employer in the long run would probably have to hire another copy reader because continuing to assign involuntary overtime for a long period of time was not desirable; and (3) the involuntary assignment of other copy readers to work on Saturday to substitute for the employee when they had seniority over the employee would cause serious morale problems among the copy readers.

However, in Draper v. United States Pipe & Foundry Co., 527 F.2d 515 (6th Cir. 1975), the court held that an employer who had fired an employee because he would not work on Saturdays violated Section 701(j) of the Civil Rights Act of 1964. The court rejected the argument of the employer that it had made a reasonable accommodation of the employee's religious practices by offering to facilitate the transfer of the employee, an electrician, to a projection job, and stated that

while in certain circumstances such a transfer might be an adequate accommodation, in the instant case the transfer would have meant a substantial reduction in pay, would have wasted the skills of the employee and there still would have been no assurance that Saturday work would not be required; therefore, the employer had to first attempt to accommodate the employee within his then current job classification.

The court stated that a shift exchange would have eliminated the problems. It found that shift exchanges could have been done without increasing labor costs and the company had a right to make shift assignments under the collective bargaining agreement. The court further noted that the employee could have made up the lost work at another time which would have left the maintenance department shorthanded for part of Saturday, but the record indicated that the department often operated with less than 15 electricians. The court therefore concluded that a reasonable accommodation of Draper's religion was possible.

Additionally, the court in Draper stated it was somewhat skeptical of hypothetical hardship that an employer thinks might be caused by an accommodation that has never been put into practice and that the record did not establish that accommodating the employee's religious practice would have caused chaotic personnel problems since ideally the substitution could be done on a voluntary basis or the Saturday work could have been rotated among all the other employees. The court rejected the argument that accommodation would cause safety problems by making electricians work more than 8 hours a day, though conceding that those safety considerations were highly relevant in determining whether a proposed accommodation would produce an undue hardship on the employer's business, since Title VII does not require that safety be subordinated to the religious practices of employees. But the court stated that the company had not sustained its burden of proving that the employee could not have been accommodated without jeopardizing safety as the record indicated that for a variety of reasons maintenance employees often work more than 8 hours per day. The court stated that it was also not convinced by the argument that to accommodate the employee would be to prefer him in violation of the overtime allocation provisions or the collective bargaining agreement because the employer had the right to direct the work force and to assign employees to shifts without regard to seniority and a partial shift exchange would not have resulted in a disproportionate assignment of overtime to the employee or a reduction in the amount of overtime available to the other employees and there was no indication that the union would object to the shift change assignment as long as 16-hour days were not scheduled on a regular basis. However, one should note that the authority of the United States Pipe case as a precedent would seem to be limited in view of the fact that it was decided prior to the decision of the Supreme Court in TransWorld Airlines v. Hardison, supra.

Recently, the court in Cowan v. Gillless, 81 F.3d 160 (6th Cir. 1996) held that an employer had reasonably accommodated the desires of an employee not to work on her Sabbath by (1) permitting her to secure a substitute for her shift any time she was scheduled to work on her Sabbath and to use the employee bulletin board to notify co-workers of her interest in swapping shifts when necessary. In the face of this evidence, the court stated that the employer was required, yet failed, to submit significant probative evidence in support of her claims in order to defeat the defendant's motion for summary judgment. The court found she could not defeat the employer's motion for summary judgment by challenging the policy as unreasonable merely because her private religious

belief had to be made public since Title VII does not require employer's to accommodate the religious practice of employees in exactly the way employees would like to be accommodated.

VI. WHEN RELIGIOUS ACCOMMODATIONS CONFLICT WITH OTHER POLICIES

The local governments of Kentucky's two largest cities have enacted "fairness ordinances" which prohibit discrimination on the basis of sexual orientation. The City of Louisville first enacted such an ordinance in 1999 and the Lexington-Fayette County combined government, which includes the city of Lexington, has followed suit. These ordinances have been interpreted as broadening the scope of existing state and federal civil rights law. There is no federal or statewide legislation in Kentucky or Tennessee that presently prohibits discrimination against gays and lesbians. However, employers should be aware that such legislation exists on the local level. There are now statewide laws in 10 states¹² and over one hundred local ordinances in twenty-seven states¹³ prohibiting the discrimination on the basis of sexual orientation or gender identity.

As the result of such legislation, prudent employers may find themselves stuck between a rock and a hard place. Employers seeking to comply with the requirements of the fairness ordinances may face opposition from other employees who argue that such prohibitions unconstitutionally infringe on their right to freedom of religion. For example, some employees may object on religious grounds to diversity and/or sensitivity training that includes a discussion of the homosexual lifestyle or other measures employers take to comply with "fairness ordinances."

In Altman v. Minnesota Department of Corrections, 251 F.3d 1199 (8th Cir. 2001), employees of the Minnesota Department of Corrections silently read their Bibles during a mandatory seventy-five minute training program entitled "Gays and Lesbians in the Workplace." The employees received written reprimands, which made two of the employees ineligible for promotions then in progress. Said employees then filed this action against the Department alleging that the reprimands violated their federal and state constitutional rights of free speech, free exercise of religion, and freedom of conscience, their right to equal protection, and Title VII.

The district court granted summary judgment dismissing the employees' free speech, equal protection and Title VII claims. The employees appeal those rulings. The court upheld their free exercise and freedom of conscience claims and granted the employers qualified immunity on those damage claims and ordered them in their official capacities to withdraw the written reprimands. The employees appealed the grant of qualified immunity. The employer cross-appealed the grant of any relief on the free exercise and freedom of conscience claims. The Court of Appeals for the Eighth

¹² These include: California, Connecticut, Hawaii, Massachusetts, Minnesota, New Hampshire, New Jersey, Rhode Island, Vermont, Wisconsin, and the District of Columbia.

¹³ States with local ordinances include Alaska, Arizona, Colorado, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Louisiana, Maine, Maryland, Michigan, Missouri, New Mexico, New York, North Carolina, Ohio, Oregon, Pennsylvania, South Carolina, South Dakota, Texas, Utah, Virginia, Washington, and West Virginia.

Circuit found that the employees raised triable free speech, equal protection, and Title VII issues and accordingly reversed the ruling of the district court.

The court began its analysis by discussing the employees free speech, equal protection, and Title VII claims. The court stated that to prevail on a First Amendment claim, the employees would have to prove they were punished for conduct that “fairly characterizes as constituting speech on a matter of public concern,” Id. quoting Connick v. Myers, 461 U.S. 138, 146, 103 S.Ct. 1684, 75 L.Ed.2d 708 (1983), and that their interest in speaking out on that matter of public concern “outweighs the public employer’s interest in promoting its efficiency by prohibiting the conduct.” Id. quoting Dunn v. Carroll, 40 F.3d 287, 291 (8th Cir. 1994). The employees argued that their right to equal protection of the law was violated because the defendants had not disciplined similarly situated employees who had been inattentive for other reasons during previous training sessions. In their Title VII claim, they alleged they were impermissibly disciplined on the basis of their religious beliefs. The court found that these claims raised “genuine, interrelated issues of material fact.” Id. at 1202.

The court disagreed with the district court’s ruling that the employees did not engage in speech on a matter of public interest and concern because they were “concerned only with internal policies or practices which are of relevance only to the employees of that institution.” Finding that although the issue is inherently “internal,” the court concluded that the way in which the Department deals with issues of gays and lesbians in the workplace affects the performance of their public duties and is a matter of general public concern. Additionally, the court found that summary judgment was inappropriate because a trial might establish that the reason for the discipline was the employees’ “nondisruptive speech, or their religion, or the fact that they expressed opposition through religious activity, and that other employees went unpunished who showed equally insubordinate but less constitutionally protected disregard for training.” Id.

In discussing the employees’ free exercise of religion and freedom of conscience claims, the court stated that to prevail on this claim, they must show first “that the governmental action complained of substantially burdened their religious activities.” Id. at 1204 quoting Brown v. Polk County, 61 F.3d 650, 658 (8th Cir. 1995) (en banc). The court found that neither the employees nor the district court identified a significant burden on their religion in this case. The employees did not suggest that their religion requires them to read the Bible while working. The court found that the only burden placed on the employees was a requirement that they attend a seventy-five minute training program and concluded this was not a substantial burden on their free exercise of religion.

Thus, the Court of Appeals held that: (1) employees’ conduct constituted speech on a matter of public interest; (2) fact issues remained as to state’s motive in reprimanding employees; and (3) the state did not impose significant burden on employees’ exercise of religion.

Altman operates as red flag that employers must be sensitive to their employees’ religious rights. An employer must do so but still comply with the requirements of local ordinances mandating fairness in disregard to sexual orientation and gender identity through appropriate measures. An employer who fails to reasonably accommodate an employee who raises objection

to such measures in light of Altman may be subject to potential liability under Title VII, the First Amendment and the Fourteenth Amendment.

VII. CONCLUSION

Based on the above summary of recent court decisions regarding reasonable accommodations, the state of the law appears to adhere to the general principles that employers have an affirmative duty to reasonably accommodate unless it imposes an undue hardship and employees have a good faith duty to accommodate his or her needs to the means offered by the employer. As of today, the courts have refused to require an employer to "reasonably accommodate" beyond the traditional two ways: (1) changing the working condition or (2) transferring the employee to a comparable position. Additionally, the courts have rejected arguments that there is no need to show an adverse employment action to establish a religious discrimination claim under Title VII. Finally, courts have refused to apply the reasonable accommodation test beyond its traditional scope in which an employer is only required to accommodate when the performance of job duties directly conflict with an employee's sincere religious beliefs.

Kentucky's state courts use the traditional tests for determining what is a "reasonable accommodation" but appear to set a higher bar for "undue hardship" than do the federal courts.

**THE EMPLOYER'S DUTY TO ACCOMMODATE
AN EMPLOYEE'S RELIGIOUS BELIEFS
(Slides)**

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CASE STUDY

CONVICTION VS COMMERCE

Your company is large enough to be covered by both Title VII and the Kentucky Civil Rights Act. One of your employees advises you that he has recently converted to a religion that observes a Saturday sabbath; therefore, he will no longer work on Saturdays, in conformity with his new faith's tenets.

If you allow this employee to have every Saturday off, the other members of his work crew will have to work additional Saturdays, or someone else will have to be called in to work overtime, at additional expense to the company.

What should you do?

ANALYSIS

1. Recognize that the courts will not inquire too deeply into what constitutes a sincerely held religious belief, and that the employee's religion need not be mainstream to qualify him for an accommodation.
2. Evaluate the situation using an "undue hardship" analysis.
3. Remember that the courts favor the flexible party.

Title VII and the Courts Define "Religion" Broadly

- "Religion" includes all aspects of religious observance, practice, and belief.
- Courts have recognized "Old Catholicism", the Black Muslim faith, Wicca, and atheism as "religions."
- A broad definition of "religion" minimizes the need for judicial decisions about whether particular beliefs or practices qualify as "religion" in order to avoid excessive entanglement of church and state as prohibited by the First Amendment.

FOWLER V. RHODE ISLAND, 345 U.S. 67, 70 (1953)

"it is no business of the courts to say...what is a religious practice or activity."

The test for Determining What is "Religious" Under Title VII

1. The belief for which protection is sought must be "religious" in the person's own scheme of things.
2. The belief must be sincerely held.

E.g. Welsh v. United States, 398 U.S. 333 (1970); United States v. Seeger, 380 U.S. 163 (1969)

CASE STUDY

Redmond v GAF Corporation, 574 F. 2d 897 (1978)

Facts

Redmond began working for GAF in 1953 and joined the Jehovah's Witnesses in 1958. In 1959, the church elders appointed him head of the Tuesday evening bible study class.

In 1974, the elders told Redmond the Tuesday evening class would meet on Saturday morning. Redmond took this to be a dictate of the elders.

Redmond told his supervisors he could not work on Saturday mornings, they responded that he would have to. When he did not report, they fired him.

Result:

- **The court rejected GAF's argument that no accommodation was necessary because Redmond's religion did not forbid all work on Saturday.**
- **The court concluded that GAF was on adequate notice of Redmond's conflict, but made no effort to accommodate him.**
- **The court concluded that GAF had not shown that scheduling Redmond off on Saturdays would have caused it to underman its crew, expend additional money by hiring a replacement, or contravene a collective bargaining agreement; thus, there was no undue hardship.**

The Employee's Credibility is Key

- **EEOC v Union Independiente De La Autoridad de Acueductos, 279 F. 3d 49 (1st Cir. 2002)**

- ▶ Employee Cruz, a Seventh Day Adventist, says his religion prevents him from joining the union. It's a closed shop.
- ▶ The union doubts Cruz's sincerity, since he objects only to certain membership requirements, and refuses any form of union membership only after the union offers to accommodate his original objections.

Result:

Cruz loses. The court cautions care "in separating the verity and sincerity of an employee's beliefs in order to prevent the verdict from turning on the factfinder's own ideas of what a religion should resemble," but concluded that while the "truth" of a belief is not open to question, whether the employee sincerely holds the belief is a fair subject for inquiry.

Cruz's Spectacular List of Noted Inconsistencies with his Professed Piety:

- Lying on his job application
- Divorcing his wife
- Taking an oath before a notary upon becoming a public employee, contrary to Adventist doctrine
- Working only five days a week instead of the six, contrary to Adventist doctrine

Personal Preferences Aren't Protected

(Not a promising issue for Summary Judgment)

- *Vetter v Farmland Industries, Inc., 120 F. 3d 749 (8th Cir. 1997)*
 - ▶ Vetter sues when Farmland fires him for refusing to move his trade territory, claiming he must live in Ames, which has a synagogue and an active Jewish community, rather than Webster City, which doesn't.
 - ▶ However, Vetter had agreed at interview to move to Webster City, had previously lived in a city with no synagogue, and preferred housing and schools in Ames.

CAVEAT:

The court upheld a jury verdict, noting that the evidence was conflicting. Defendant was able to get an instruction saying that Vetter had to demonstrate a sincere religious belief rather than a purely personal preference.

The Employee's Responsibilities

1. The employee must notify the employer that she needs an accommodation for a sincerely held religious belief.
2. The employee must be flexible in working toward a suitable accommodation.

Case Study

Bruff v North Mississippi Health Service, Inc., 244 F. 3d 495 (5th Cir. 2001)

Facts

- Bruff worked as a counselor for Health Service's EAP program.
- Bruff's client Jane Doe asks for Bruff's advice on issues with Doe's lesbian partner.
- Bruff declines. Doe complains.
- Bruff explains to Health Services that the subject offends her religious beliefs.

Outcome

- Health Services offers accommodations: accept Christian counselor position; or request transfer and obtain other position w/in 30 days.
- Bruff refuses, insists on having backup counselor for issues that offend her, is fired and sues.
- Jury awards Bruff compensatory and punitive damages.
- Appellate court reverses, finding Bruff was inflexible in her demand for accommodations, and that providing the backup counselor would be undue hardship.

What's an "undue hardship" in this context?

Transworld Airlines v Hardison, 432 U.S. 63 (1977)

- An undue hardship exists as a matter of law when an employer incurs more than a minimal cost to reasonably accommodate an employee's religious beliefs.
- The accommodation given does not have to be the one the employee prefers.

CASE STUDY

ON THE ROAD AGAIN

A male truck driver learns that some of the drivers to be assigned for overnight hauls with him are female. He objects on religious grounds. His supervisor says "too bad." The trucker protests that other drivers are sometimes allowed to decline assignments in case of emergencies; therefore, he should be allowed to decline assignments with female truck drivers. Should this request be accommodated?

ANSWER

No. In Weber v Roadway Express, 199 F. 3d 370 (5th Cir. 2000), the court concluded that Weber's standing request was inflexible, that it was different from the occasional requests of other drivers with emergencies, and that accommodating Weber would inconvenience other drivers, which was itself an undue hardship. The court also rejected Weber's attempt to impose the ADA's higher standard for proving "undue hardship" upon employers in the context of disputes about accommodating religious beliefs.

CASE STUDY

HAVE A BLESSED DAY!

Anderson v U.S.F. Logistics, 274 F. 3d 470 (7th Cir. 2001)

Anderson ends her business conversations and letters with "have a blessed day." U.S.F.'s biggest customer, Microsoft, complains. Anderson is warned not to use this phrase with customers. An article appears in the newspaper in which Microsoft denies that it had any problem with Anderson's business blessings, so Anderson deliberately resumes using the phrase in her business conversations and letters. U.S. F. fires her.

How will this come out?

- The court concluded that U.S. F. reasonably accommodated Anderson because:
 - ▣ She was allowed to say "Have a blessed day" to everyone except customers.
 - ▣ U.S.F. did not object to Anderson's other religious practices.

CASE STUDY

George v Home Depot, Inc., 82 EPD 40881 (E.D. La. 2002)

Home Depot hires George as a greeter, expecting her to work peak weekend hours. George refuses to work on Sundays, saying her religion (Catholic) requires her to rest

mind and body on Sundays. She offers to work on Saturday instead. Home Depot refuses to give her every Sunday off, but agrees to arrange her weekend schedule so that she could attend Mass. George refuses and gets fired.

Did Home Depot offer a reasonable accommodation?

ANSWER

Yes. The court concluded that George was inflexible in refusing any accommodation other than one on the exact terms she demanded. Home Depot demonstrated that it would have suffered undue hardship in giving her every Sunday off because designers would have had to perform George's job duties, thus reducing her department's efficiency; and other employees' schedules would suffer. (N.B. Compare Redmond, where the employer failed to make this vital showing).

What is an "adverse employment action" that will support a failure to accommodate claim?

Ali v Alamo Rent-a-Car

Ali, a management trainee and a Muslim, works at Alamo's front desk. Her supervisor tells her she must remove her hejab or transfer away from public view. She refuses to remove the scarf and gets transferred. The Fourth Circuit concludes that the transfer did not affect compensation, terms, conditions, or privileges of employment.

The "Religious Institution" Exception

- Title VII exempts bona fide religious institutions from claims of discrimination based upon religion
- The "religious institution" exception is not waivable

CASE STUDY

Hall v Memorial Health Care Corp., 215 F. 3d 618 (6th Cir. 2000)

Memorial Healthcare is affiliated with the Southern Baptist Convention, which has been outspoken in its views against homosexuality. Hall, a student services specialist, became an ordained minister in a church that taught that homosexuality does not conflict with Christian principles.

What happened next....

- Memorial asked Hall to resign or look for a job that involved less contact with students.
- Hall refused.

- Memorial fired Hall, claiming conflict of interest.

Then came the lawsuit...

- The court concluded that Memorial was a bona fide religious institution.
- The court rejected Hall's argument that Memorial had waived its religious institution exemption by claiming to be an equal opportunity employer, or by receiving federal funds.
- The court rejected Hall's attempt to spin the case as one of "reasonable accommodation" as opposed to what it was: a disparate treatment case.
- The court pointed out that the employer never asked Hall to do anything that conflicted with her religious beliefs, and in any event, offered reasonable accommodation.

Kentucky Decisions

Hazlewood: Hospital failed to accommodate nursing aid trainee who accepted job then told employee she could not work on Sundays. Court acknowledges U.S. Supreme Court decision in Hardison, but says it is not controlling. Concludes that hospital should have looked into letting plaintiff switch times with other employees in addition to letting her apply for other jobs.

Kentucky Decisions (cont)

Kerns Bakery: court sides with a baker who refuses to bake on Sunday, saying the employer should have offered him another job or just let him skip Sundays.

Evans: emergency room did not violate KRS Chapter 344 when it fired an employee who refused to work on Saturdays (his Sabbath) when he could no longer find a replacement.

Irvin: (not final) public employer not required to accommodate employee who is also a minister when employee applies for a job that requires Sunday work, then refuses Sunday work.

Final Query: What if one person's idea of fairness is another person's idea of oppression?

- Ten states and a hundred local jurisdictions (including Lexington-Fayette County) have laws or ordinances forbidding employment discrimination based upon sexual orientation.
- What if an employer wants to conduct sensitivity training about this subject, but some employees protest that attending would violate their religious beliefs?



**WORKPLACE HARASSMENT:
A CRITICAL UPDATE**

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SECTION E



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I. Introduction

In 1998, the United States Supreme Court issued three ground-breaking decisions in the field of workplace harassment: Oncale v. Sundowner Offshore Services, 523 U.S. 75 (1998); Burlington Industries v. Ellerth, 524 U.S. 742 (1998) and Faragher v. City of Boca Raton, 524 U. S. 775 (1998). Oncale made clear that same-sex sexual harassment is actionable under Title VII of the Civil Rights Act of 1964 and Faragher and Ellerth established the circumstances under which employers will be liable for harassment committed by supervisors and managers.

This trio of cases has resulted in an avalanche of federal district and circuit court decisions further defining and refining the parameters of sexual and other types of harassment. Although the United States Supreme Court has continued to speak in the harassment area, its more recent cases have had more limited application. In Pollard v. E.I. du Pont de Nemours, 532 U.S. 843 (2001), for example, the Supreme Court held in a hostile environment sexual harassment case that front pay was not an element of compensatory damages within the meaning of the Civil Rights Act of 1991, and therefore not subject to the Act's statutory damage caps. In Clark County School District v. Breeden, 532 U.S. 268 (2001), the Supreme Court held that no reasonable person could have believed that a single relatively mild incident of alleged sexual harassment violated Title VII, thus precluding a retaliation claim based on the employee's internal complaint.

Although the overwhelming majority of workplace harassment cases continue to allege sexual and racial harassment, courts have more recently begun to recognize national origin and religious-based harassment (under Title VII) and age and disability-based harassment (under the ADEA and ADA, respectively).

Kentucky state courts continue to consider and follow federal court decisions under Title VII when interpreting and applying the Kentucky Civil Rights Act. The Kentucky Supreme Court has shown its willingness to adapt the Faragher and Ellerth supervisor liability standards and has recently issued an important case demonstrating a broad interpretation of the employer's duty to promptly correct harassing behavior.

As the following outline will show, workplace harassment remains a heavily litigated and constantly evolving area of employment law.

II. The Statutory Basis for the Prohibition of Harassment

A. The Civil Rights Act of 1964 (Title VII), 42 U.S.C. §2000e (as amended)

1. Prohibited Conduct

The Civil Rights Act of 1964, Title VII, 42 U.S.C. § 2000e, *et seq.*, ("Title VII") provides that it is unlawful for an employer to "fail or refuse to hire or to discharge any individual, or otherwise discriminate against any individual with respect to his compensation, terms, conditions or privileges of employment, because of such individual's race, color, religion, sex or national origin." 42 U.S.C. § 2000e-2(a)(1). In holding that a plaintiff may establish a violation of Title VII by

proving that discrimination based on sex has created a hostile or abusive working environment, the United States Supreme Court, in Meritor, 477 U.S. at 66, suggested that harassment based on race, color, religion and national origin might likewise be actionable.

Two types of sexual harassment have been recognized by the Courts: (1) harassment which creates a hostile work environment, and (2) *quid pro quo* harassment, where an employee's supervisor makes the receipt of tangible job benefits contingent upon submission to unwelcome sexual advances. The distinctions between hostile environment and *quid pro quo* sexual harassment, while still recognized, do not have the same significance as they did before Burlington Industries, Inc. v. Ellerth, 524 U.S. 742, 118 S.Ct. 2257 (1998).

2. Remedies

Remedies available in Title VII cases are provided by 42 U.S.C. § 1981a and § 2000e-5(g)(k). 42 U.S.C. § 2000e-5(g) provides:

If the court finds that the respondent has intentionally engaged in . . . [a discriminatory] employment practice, . . . the court may enjoin the respondent from engaging in such unlawful employment practice, and order such affirmative action as may be appropriate, which may include, but is not limited to reinstatement, . . . back pay, . . . or any other equitable relief the court deems appropriate.

42 U.S.C. § 2000e-5(k) provides for the recovery of attorneys' fees by the prevailing party. Section 1981a provides for the recovery of compensatory damages not otherwise available, and for the recovery of punitive damages. However, the amount of punitive and actual damages that are recoverable under §1981a is capped depending upon the defendant's total number of employees, with a maximum amount of \$300,000 for employers with more than 500 employees. The Sixth Circuit has ruled that this cap does not apply to each separate claim made by an individual, but represents the total aggregate amount which can be recovered, regardless of the amounts awarded for each individual claim, and regardless of the number of claims on which the plaintiff prevailed. Hudson v. Reno, 130 F.3d 1193 (6th Cir. 1997) *abrogated on other grounds* by Pollard, 532 U.S. 843. Attorneys' fees, back pay and front pay awards are not subject to the caps.

3. Punitive Damages

The U.S. Supreme Court clarified the standard for recovery of punitive damages in Title VII cases, in Kolstad v. American Dental Ass'n., 527 U.S. 526 (1999). In this case, Kolstad challenged her employer's decision to promote a male to a position she also sought. She claimed that the selection process was a sham, and that the reason offered by the employer for its decision to promote the male was a pretext for gender discrimination. At trial, the judge refused to allow a jury instruction on punitive damages. After the jury returned a verdict in Kolstad's favor, she appealed the trial court's denial of her request for a punitive damages instruction. The appellate court upheld the trial court's decision, finding that punitive damages were only warranted in cases where the plaintiff could demonstrate that the employer engaged in "egregious" misconduct.

The Supreme Court rejected this standard, and provided a two-part test for awarding punitive damages. First, punitive damages can only be recovered if the plaintiff demonstrates that the employer or its agent engaged in "intentional discrimination." Intentional discrimination occurs when the employer or its agent knowingly bases an employment decision on the individual's membership in a protected class. Although a plaintiff may recover actual or compensatory damages in cases of both intentional and unintentional discrimination (such as claims that a policy or practice has a disparate impact on a particular class, and is not justified by business necessity), a plaintiff can only proceed to the next level of analysis if he or she can show that the employer or agent consciously made a decision based on prohibited considerations.

Next, the plaintiff must show that the employer or its agent acted with malice or reckless indifference to the fact that the discrimination might violate the plaintiff's rights under federal law. The Court explained that this is a separate analysis from determining whether the decision-maker was consciously influenced by the employee's protected status. The requirement of "malice" or "reckless indifference" relates to the employer's knowledge that it may be acting in violation of law, not its awareness that it is engaging in discrimination. This second prong focuses on the mental state of the individual making the discriminatory decision. The Court noted that there will not always be an overlap between the employer's awareness that it is engaging in discrimination, and the awareness that the discrimination may violate federal law. The Court recognized that there may be cases where the employer is unaware of a relevant federal prohibition, where the employer or its agent may, in good faith, believe that making a decision based on a disability or other protected characteristic is not unlawful, or cases where the theory of discrimination advanced by the plaintiff is novel or not generally accepted. However, the Court cautioned against reliance on deliberate ignorance of the law as a defense to punitive damages.

In order to encourage employers to adopt policies and practices designed to end unlawful discrimination, the Court created a safe harbor that may allow an employer to limit or even completely avoid liability for punitive damages based on intentional discrimination by a managerial agent. The Court recognized that an employer will not be vicariously liable for punitive damages due to the acts of its managerial agents where the employer has made a good faith effort to prevent discrimination in the workplace. The examples of good faith efforts specifically mentioned by the Court include the existence of a written policy prohibiting discrimination that has been instituted in good faith and the implementation of programs or other policies to prevent discrimination in the workplace.

B. The Civil Rights Act of 1991, 42 U.S.C. § 1981 (as amended).

1. Prohibited Conduct

The Civil Rights Act of 1866, 42 U.S.C. § 1981, was enacted to provide all persons within the jurisdiction of the United States with the same rights to make and enforce contracts, to sue, be a party to a lawsuit, to testify in a legal proceeding, and have the full and equal benefit of all laws protecting their person and property regardless of their race. Prior to its 1991 amendment, the United States Supreme Court interpreted § 1981 in an employment context as only providing a remedy for

hiring decisions, sometimes referred to as “pre-formation” conduct, based on race. As a result, it provided no remedy for race discrimination, such as racial harassment, which occurred during the course of the employment relationship. Patterson v. McLean Credit Union, 491 U.S. 164 (1989).

In 1991, Congress amended § 1981 to provide that the power to “make and enforce contracts” includes “the making, performance, modification, and termination of contracts, and the enjoyment of all benefits, privileges, terms, and condition of the contractual relationship.” 42 U.S.C. § 1981(b). This statute is now construed broadly by the courts to prohibit discrimination in any of the terms and conditions of employment on the basis of race, at all stages of the employment relationship. Williams v. Carrier Corp., 889 F. Supp. 1528 (M.D.Ga. 1995); Allen v. City of Chicago, 828 F. Supp. 543 (N.D. Ill. 1993).

2. Remedies

Although § 1981 does not contain specific remedies provisions, both compensatory and punitive damages have been awarded under § 1981. There are no damages caps for claims brought under § 1981. Accordingly, most claims for racial harassment are often pled as both Title VII and § 1981 causes of action.

C. The Kentucky Civil Rights Act

1. Prohibited Conduct.

The Kentucky Civil Rights Act (“KCRA”), KRS § 344.010 *et seq.*, was enacted to provide for execution within Kentucky of the policies embodied in federal anti-discrimination statutes. “Kentucky’s Civil Rights Act was enacted to in a measure enforce policy established in federal civil rights law.” McNeal v. Armour & Co., 660 S.W.2d 957, 959 (Ky. App. 1983) (*citing* KRS § 344.020). The KCRA incorporates the policies of the federal Civil Rights Act of 1964, as amended (78 Stat. 241), Title VIII of the federal Civil Rights Act of 1968 (82 Stat. 81), the Fair Housing Act, as amended (42 U.S.C. § 360), the federal Age Discrimination in Employment Act of 1967 (81 Stat. 602), and the Americans with Disabilities Act of 1990 (P.L. 101-336). *See* KRS 344.020(1)(a).

Because the KCRA is modeled on federal legislation, decisions interpreting these federal statutes are considered highly persuasive by the Kentucky courts. Mountain Clay, Inc. v. Commonwealth Commission on Human Rights, 830 S.W.2d 395, 396 (Ky. App. 1992); Kentucky Commission on Human Rights v. City of Owensboro, 750 S.W.2d 422, 423 (Ky. 1988); White v. Rainbo Baking Co., 765 S.W.2d 26, 28 (Ky. App. 1988); McNeal v. Armour and Co., 660 S.W.2d 957 (Ky. App. 1983); Kentucky Commission on Human Rights v. Commonwealth, Dept. of Justice, 586 S.W.2d 270, 271 (Ky. App. 1979).

2. Remedies

The KCRA provides for recovery of actual damages sustained by the plaintiff, together with the costs of the lawsuit, including a reasonable attorney's fee for the plaintiff's attorney of record. KRS § 344.450.

In Meyers v. Chapman Printing Co., 840 S.W.2d 814, 817 (Ky. 1992), the Kentucky Supreme Court recognized that while the KCRA incorporates the anti-discrimination policies embodied in Title VII, it also contains further protections not specified in Title VII, including "protect[ing] . . . personal dignity and freedom from humiliation." Accordingly, the courts have allowed successful plaintiffs to recover compensatory damages under this statute, including damages for "embarrassment and humiliation."

The KCRA does not contain a damages cap.

3. Punitive Damages.

At the time this publication is going to press, the question of whether punitive damages may be awarded under the KCRA is unresolved. In an opinion since ordered depublished, the Kentucky Court of Appeals, in Union Underwear Co., Inc. d/b/a Fruit of the Loom v. Barnhart, upheld the trial Court's instruction to the jury on the issue of punitive damages in an age discrimination case. The case was reversed on other grounds in Union Underwear v. Barnhart, 50 S.W. 3d 188 (Ky. 2001), *reh'g denied* (2001), with no mention of the punitive damage issue. The United States District Court for the Western District of Kentucky, in Timmons v. Wal-Mart Stores, Inc., 33 F.Supp. 2d 577 (W.D. Ky. 1999), found that the KCRA permits punitive damages, while the United States District Court for the Eastern District of Kentucky and the Sixth Circuit have found that punitive damages are *not* authorized by the act. Messick v. Toyota Motor Mfg., Ky., Inc., 45 F.Supp.2d 578 (E.D. Ky. 1999); Lewis v. Quaker Chemical Corp., 229 F.3d 1152, (6th Cir. 2000). The Kentucky Court of Appeals, in Kentucky Dept. of Correction v. McCullough, 2000 WL 707953 (Ky. App. 2000), *disc. review granted* Feb. 14, 2001 (unpublished opinion) agreed with Timmons, *supra*, that punitive damages *are* recoverable under the KCRA. This question will presumably soon be put to rest by the Kentucky Supreme Court, as it has granted discretionary review in McCullough.

III. Sexual Harassment

A. Hostile Work Environment Harassment.

The most recognized type of unlawful harassment is "hostile work environment harassment." This type of harassment does not directly affect an economic aspect of the victim's employment, such as promotion, discharge or salary, but rather deprives an employee of the right to work in an environment free from discriminatory intimidation, ridicule and insult.

1. Required Elements of the Plaintiff's Claim.

A cause of action charging a sexually hostile work environment is evaluated in the Sixth Circuit using the five part test set forth in Rabidue v. Osceola Refining Co., Div. of Texas American Petrochemicals, 805 F.2d 611 (6th Cir. 1986) *abrogated on other grounds by Harris*, 510 U.S. 17. Generally, to prevail in a Title VII hostile work environment sexual harassment action, an employee must assert and prove that:

- (1) the employee is a member of a protected class;
- (2) the employee was subjected to unwelcome sexual harassment;
- (3) the harassment complained of was "based on sex";
- (4) the harassment had the effect of unreasonably interfering with the plaintiff's work performance and creating an intimidating, hostile or offensive work environment (or alternatively was "sufficiently severe or pervasive" so as to create a hostile or abusive work environment);
- (5) the existence of employer liability.

Fleenor v. Hewitt Soap Co., 81 F.3d 48 (6th Cir. 1996); Harris, 510 U.S. 17.

a. The Plaintiff Must Be A Member of a Protected Class.

Although the plaintiff's work environment may be affected due to sexual harassment directed at others (see next section), the plaintiff generally will not be permitted to recover under the hostile environment theory unless that plaintiff and the targets of harassment are members of the same class. Accordingly, a male employee cannot recover under the hostile environment theory based on a claim that his work environment has been affected due to his distress over the pervasive harassment of females in his department. *See, e.g., Leibovitz v. New York City Transit Authority*, 252 F.3d 179 (2nd Cir. 2001); Childress v. City of Richmond, 134 F.3d 1205 (4th Cir. 1998).

b. The Plaintiff Was "Subjected to" the Conduct.

In Hicks v. Gates Rubber Co., 833 F.2d 1406 (10th Cir. 1987), the court examined whether sexual harassment directed at employees other than the plaintiff can be used as proof of the plaintiff's claim of a hostile work environment, and stated: "The answer seems clear: one of the critical inquiries in a hostile environment claim must be the *environment*. Evidence of a general work atmosphere therefore - - as well as evidence of specific hostility directed toward the plaintiff - - is an important factor in evaluating the claim." *Id.* at 1415, *citing Vinson v. Taylor*, 753 F.2d 141 (D.C. Cir. 1985), *aff'd in part and reversed in part*, 477 U.S. 57 (1986).

The Hicks opinion suggests that it is not necessary for the plaintiff to show that *any* sexual harassment was directed specifically toward her in order to state a cognizable hostile environment claim under Title VII. “Even a woman who was never herself the object of harassment might have a Title VII claim if she were forced to work in an atmosphere where such harassment was pervasive.” *Id.* at 1416. *See also Sims v. Montgomery County Commission*, 766 F. Supp. 1052 at 1074 (M.D. Ala. 1990) (in refusing to limit the remedy for harassment to only the persons at whom it was directed, the court explained that under Title VII, a person may be a victim of sexual harassment without being its intended victim; the challenged conduct need not be directed at the complaining individual); Broderick v. Ruder, 685 F. Supp. 1269 at 1277-78 (D.D.C. 1988) (women forced to work in an atmosphere pervaded by harassment may have a Title VII action even if they suffered no harassment themselves).

Note that, under a hostile work environment theory, actionable harassment may be committed by supervisors, co-workers or other individuals present in the workplace, such as customers.

c. The Conduct Was Unwelcome

The most fundamental aspect of actionable sexual harassment is that the sexual conduct was unwelcome. An employee must show that he or she did not solicit or invite the conduct, regarded the conduct as undesirable or offensive, and also that the harasser knew or should have realized that the conduct was unwelcome. This notice may be actual or constructive. Bales v. Wal-Mart Stores, Inc., 143 F.3d 1103 (8th Cir. 1998). The fact that the employee may have freely consented to, or participated in such conduct in the past will not necessarily defeat the employee’s claim, if the employee can show that he or she later made it clear to the alleged harasser that the conduct was no longer welcome. Burns v. McGregor Electronic Industries, Inc., 989 F.2d 959 (8th Cir. 1993) (The fact that the plaintiff posed for a pornographic magazine did not mean that she “welcomed” repeated sexual advances and vulgar comments about pictures in the magazine while she was at work.)

Further, a plaintiff’s voluntary submission to sexual conduct will not necessarily defeat a claim of harassment. The crux of a sexual harassment claim is that the alleged sexual advances were “unwelcome” not that the complainant was forced to participate against her will. Meritor, 477 U.S. at 68.

d. The Conduct Was “Based on Sex”

Conduct that is “based on sex” may be sexual in nature, such as requests for sexual favors and comments about sexual activity. However, the key issue is not whether the conduct was about sex, but rather, whether the conduct would not have occurred but for the employee’s sex. Williams v. General Motors Corp., 187 F.3d 553 (6th Cir. 1999). Unless the victim is able to show that a supervisor, co-worker, etc. mistreated one sex but not the other, or directed the complained of behavior at the victim *because* of his or her gender, then the harassment has not occurred “because of sex,” and he or she should not be able to prevail on the claim. EEOC v. Harbert-Yeargin, 266 F.3d 498 (6th Cir. 2001) (Where only three of 292 employees were women, and none of the women worked in the field with the male plaintiffs, court could not conclude that “gross, vulgar, male horseplay” was directed at plaintiff because of his sex).

The gender and the sexual orientation of the harasser are not relevant to the claim. Oncale v. Sundowner Offshore Services, 523 U.S. 75 (1998); *see also* Brewer v. Hillard, 15 S.W.3d 1 (Ky. App. 1999) (applying Oncale to hold that same sex harassment is actionable under the KCRA). *See* § [7.50], *infra*, for a discussion of gender based harassment arising from conduct that has no sexual content.

e. The Harassment Was Severe or Pervasive

Hostile environments may be created by very different combinations and frequencies of hostile sexual conduct. However, the plaintiff generally has the burden of demonstrating that the hostile environment resulted not from a single isolated or offensive incident, comment or action, but from incidents, comments or conduct that occurred with some frequency. The allegedly harassing incidents must be “more than episodic”; they must, under the totality of the circumstances, be “sufficiently continuous and concerted” in order to be deemed pervasive. Harris, 510 U.S. at 21. Single incidents of harassment will rarely be sufficiently severe to create a hostile work environment. *See* § [7.25], *infra*.

i. Conduct Held Insufficiently Severe or Pervasive to Create Hostile Environment

The Court of Appeals for the Sixth Circuit, in Stacy v. Shoney’s, 955 F. Supp.751 (E.D. Ky. 1997) *aff’d by* 142 F.3d 436 (6th Cir. 1998) (unpublished table decision), upheld the District Court’s grant of summary judgment in favor of Shoney’s, finding that the conduct alleged failed to rise to the level required to support a finding that a hostile environment existed in violation of the KCRA.

In this case, Stacy alleged that over the course of her two months of employment with Shoney’s, her supervisor, Mr. Kimbrell, “created a hostile and abusive work environment” for her. Specifically, Stacy alleged that Mr. Kimbrell made the following “sexual” remarks to her: (1) he told her that her “hair looks better down”; (2) he said that her “tan looks good” and told her that he wished he “could see more of it”; (3) he told a dishwasher at Shoney’s that he never had a sister who looked like Stacy; (4) he made a comment to Stacy about working on the night shift with him; (5) he told her that he would move in with her and take care of her “in a heartbeat”; (6) he called Stacy at work on his days off and told her that he missed her; (7) he told her that she could have anything she wanted when she asked him for a cigarette; and (8) he told Stacy that if he had someone who looked as good as her, he would not let her out of the house. Stacy also alleged that on one occasion Mr. Kimbrell took a pen out of her shirt pocket and touched her breast with his fist. Other than this one incident of “physical contact,” Mr. Kimbrell never touched her.

Quoting from Blankenship v. Parke Care Centers, Inc., 913 F.Supp. 1045, 1051 (S.D. Ohio 1995), *cert. denied*, 522 U. S. 1110 (1998) the District Court wrote:

The concept of sexual harassment is designed to protect women from the kind of male attentions that can make the workplace hellish for women It is not designed to purge the workplace of vulgarity.

Drawing the line is not always easy. On one side lies sexual assaults; other physical contact whether amorous or hostile, for which there is no consent express or implied; uninvited sexual solicitations; intimidating words or acts; obscene language or gestures; pornographic pictures. On the other side lies the occasional vulgar banter, tinged with sexual innuendo, of course or boorish workers.

Stacy, 955 F. Supp. at 755; *see also*, Black v. Zaring Homes, Inc., 104 F.3d 822 (6th Cir. 1997) (Comments including “Nothing I like more in the morning than sticky buns, “ and “Say, weren’t you there [at the biker bar] Saturday night dancing on the tables?” and references to “Hootersville” and “Twin Peaks” held not actionable); Koelsch v. Beltone Elec. Co., 46 F.3d 705 (7th Cir. 1995) (supervisor who stroked plaintiff’s leg on one occasion, grabbed her buttocks, told her he found her attractive, and twice asked her out on a date, did not commit acts rising to the level of hostile environment sexual harassment); Morris v. Oldham County Fiscal Court, 201 F.3d 784 (6th Cir. 2000) (construing KCRA) (several dirty jokes told in plaintiff’s presence, an alleged verbal sexual advance, one-time reference to plaintiff as “Hot Lips” and isolated comments about plaintiff’s state of dress held insufficient to create hostile work environment); Burnett v. Tyco Corp., 203 F.3d 980 (6th Cir. 2000), *cert. denied* 531 U.S. 928 (2000) (single battery coupled with two offensive remarks over six months does not create a factual issue).

In EEOC v. Harbert-Yeargin, 266 F.3d 498 (6th Cir. 2001), the Sixth Circuit, in a same sex harassment case, ruled that a supervisor’s having grabbed the plaintiff in his genital area on a couple of occasions, and stalked the plaintiff by hanging around him and looking at him from a distance was “gross, vulgar, male horseplay.” However, it was not sufficient to create liability under Title VII. *Id.* at 522-523.

ii. Conduct Held Sufficiently Severe or Pervasive to Create Hostile Work Environment

When reviewing the evidence of harassment, the courts generally apply a sliding scale, *e.g.*, the more severe the conduct, the less frequently it must occur before becoming actionable. Conversely, the more frequent the conduct, the less severe it must be in order to be deemed as having altered the work environment. In Hathaway v. Runyon, 132 F.3d 1214 (8th Cir. 1997), a jury found that the evidence was sufficient to establish a hostile work environment where a co-worker touched the plaintiff only two times in a sexually suggestive manner, but after her rejection of his advances, he laughed and made suggestive noises to plaintiff for a period of eight months and repeatedly blocked her exit from their narrow workroom.

f. The Conduct Was Objectively and Subjectively Hostile or Abusive

In Harris, the United States Supreme Court held that in order for conduct to be found “sufficiently severe or pervasive to create a hostile or abusive working environment, there must be both an objective and subjective component.” Harris, 510 U.S. at 21. Conduct that is not severe or pervasive enough to create an environment that a reasonable person would find hostile or abusive is

beyond Title VII's reach. Similarly, the victim must subjectively perceive the environment to be hostile or abusive if a violation of Title VII is to be found. *Id.*

g. The Conduct Had the Effect of Altering the Work Environment

In addition to holding that there must be both an objective and subjective component to the existence of a hostile or abusive working environment, the Supreme Court in Harris refused to require that the plaintiff show an environment that seriously affected her *psychological well-being*. The Court instead reaffirmed the standard set forth in Meritor, requiring the plaintiff to show that the workplace was permeated with discriminatory intimidation, ridicule and insult that was sufficiently severe or pervasive to alter the conditions of the victim's employment and create an abusive working environment. Harris, 510 U.S. at 22-23.

h. Employer Liability

i. Liability for a Hostile Environment Created by Co-Workers or Third Parties

An employer will be liable for harassment by non-supervisory employees and for harassment committed by third parties such as customers or vendors where the employer or its agents or supervisory employees knew or should have known of the conduct, and failed to take action to end the harassment.

Since 1980, the Equal Employment Opportunity Commission ("EEOC") has stated in its Guidelines on Discrimination Because of Sex that employers may be held responsible for sexual harassment by non-employees "where the employer (or its agents or supervisory employees) knows or should have known of the conduct and fails to take immediate action." 29 C.F.R. § 1604.11(e), as amended.

In Lockard v. Pizza Hut, 162 F.3d 1062 (10th Cir. 1998), the Tenth Circuit rejected an employer's argument that it could not be held liable for harassing conduct by its customers. In this case, two male customers were well known in the restaurant, and the plaintiff, a waitress, had previously told her supervisor that she did not like to wait on them. On the day in question, the waitress was propositioned by one of the customers, and rebuffed his advance. He responded by grabbing her hair. She then went to her manager and asked that she not be required to continue to wait on their table. The manager refused her request. When she returned to their table, she was physically assaulted by one of the men. The court ruled that the employer was liable for the harassment, because it had notice of the problem and had the ability to control the waitress's working environment, but failed to do so. The court also recognized that the manager's actions violated a specific company policy that provided instructions on how to deal with harassing customers.

Similarly, the employer was held liable for harassment by a customer in Menchaca v. Rose Records, 1995 WL 151847, 67 Fair Empl. Prac. Cas. (BNA) 1334 (N.D. Ill. Apr. 3, 1995). In this case, a female employee of a record store was repeatedly harassed by one of the store's regular customers. The customer regularly made sexual comments to the employee, asked her out on dates

and to sleep with him, and he attempted to grab the employee from behind several times. Although the employee complained to the store manager about the customer's behavior, the manager still took no action. On one occasion the manager was present when the customer grabbed the employee and dangled her by her ankles, injuring her arm and tailbone. However, the manager took no action to either halt or discourage the customer's conduct. Applying the rationale found in the EEOC guidance, the district court denied the defendant's summary judgment motion, stating that "a harasser's status as a non-employee does not as a matter of law shield the employer from liability under Title VII, if the employer knew or should have known of the harassment." *Id.* at 1336-37. *See also, Rodriguez-Hernandez v. Miranda-Velez*, 132 F.3d 848 (1st Cir. 1998) (employer liable for harassment of female employee by an important client when, after complaint was made by employee, her supervisor told her to respond "as a woman" and then fired her when she refused the client's advances); *Llewellyn v. Celanese Corp.*, 693 F. Supp. 369 (W.D.N.C. 1988) (employer liable for harassment by customer where employer responded to female employee's complaint that the customer made unwanted sexual advances to employee, by stating that "the customer is always right").

ii. Knowledge Imputed to Employer

One of the questions that will be relevant to the liability of an employer for a hostile work environment caused by a co-employee or third party is whether the employer knew or should have known of the alleged harassment. Actual notice may be found if the employee complained of the harassment to the company's personnel office or other management personnel. Knowledge may be imputed to the employer if the harassment is so severe or pervasive that the employer was negligent in failing to discover and prevent it. *Baskerville v. Culligan Int'l Co.*, 50 F.3d 428, 432 (7th Cir. 1995).

In *Morrison v. Carleton Woolen Mills, Inc.*, 108 F.3d 429 (1st Cir. 1997), the employer was charged with constructive knowledge of a hostile environment, despite the plaintiff's failure to use official procedures to complain because other women had made complaints against the same alleged harasser and the layout of the mill was such that higher management "could not have missed the discriminatory atmosphere that permeated the department." *Id.* at 437- 438.

iii. Failure to Act to Remedy Harassment

Generally, an employer will have no liability for harassment by non-supervisory co-workers or third parties if it responded promptly after receiving notice of the harassment, and the response was adequate. Adequacy is usually found where the response was reasonably calculated to, or did in fact, cause the harassment to stop. However, if the harasser has already stopped all objectionable conduct voluntarily, the employer may still be liable to an employee who has reported harassment, unless the employer takes some additional action to address the past problem, and demonstrate to the harasser and the victim that the employer will not tolerate harassment in the workplace. *Fuller v. City of Oakland*, 47 F.3d 1522 (9th Cir. 1995).

In *Wathen v. General Electric Co.*, 115 F.3d 400 (6th Cir. 1997) the Sixth Circuit found that the employer was not liable for sexual harassment under either Title VII or the KCRA, where (1) the

employer had a written policy that explicitly prohibited sexual harassment, (2) immediately upon learning of the harassment the employer terminated one co-worker, severely reprimanded another, and required that public apologies be made to the victim, and (3) as a result of the employer's actions, all harassment stopped.

In Fleenor v. Hewitt Soap Co., 81 F.3d 48 (6th Cir. 1996), the employer was not held liable for hostile environment sexual harassment where the harassment by the plaintiff's co-worker was not known to the employer prior to the plaintiff's report, and immediately thereafter the employer reprimanded the co-worker and the objectionable conduct stopped. The Sixth Circuit stated that since the harassment stopped after the employer took action, the requirement that the employer's remedial action be reasonably calculated to end the harassment was satisfied. *See also*, Wilson v. Southern National Bank of North Carolina, Inc., 900 F. Supp. 803 (W.D. N.C. 1995) in which the employer was excused from liability for a hostile work environment where it had no knowledge of the harassment until the complaint was made, and it took prompt remedial action after the complaint. Actions taken by the employer to remedy the hostile environment included a departmental meeting, a memo issued to employees, and transferring the plaintiff to a new department with a raise.

In Torres v. Pisano, 116 F.3d 625 (2nd Cir. 1997), the Second Circuit reaffirmed that an employer's written policy outlawing sexual harassment coupled with prompt action to remedy an employee's claim would, except in unusual cases, defeat a hostile work environment claim on summary judgment. The Torres court also found that an employer may be relieved from its responsibility to take prompt remedial action to remedy a hostile work environment, if the employee making the report has requested that the employer not investigate the claim, keep the claim confidential, and take no action. The court suggested that the only time such a request must be dishonored is when the reported harassment involves a severe form of sexual harassment that might pose a threat of serious physical or psychological harm. However, the recent EEOC Guidance on Vicarious Liability for Harassment by Supervisors, and the Kentucky Supreme Court's decision in Bank One, Kentucky, N.A. v. Murphy, 52 S.W.3d 540 (Ky. 2001) discussed more fully in § [7.46] *infra*, provide strong support for adopting a practice that requires supervisors and managers to report and/or respond to a complaint of harassment, regardless of the circumstances under which they become aware of the allegations.

B. Quid Pro Quo Sexual Harassment

Prior to the Supreme Court's opinion in Burlington Industries v. Ellerth, 524 U.S. 742 (1998), courts drew a sharp distinction between hostile environment cases (in which employer liability usually turned on whether the employer knew or should have known of the harassment and where the plaintiff had to establish severe or pervasive conduct) and *quid pro quo* cases (in which employers faced strict liability and where a single request for sexual favors was generally sufficient to establish liability). In a *quid pro quo* case, the plaintiff complained that her supervisor or manager conditioned the receipt of job benefits on the acceptance of unwelcome sexual advances, thus ordinarily resulting in the loss of those job benefits. Such cases usually differed from hostile environment cases, in which plaintiffs often suffered no tangible job detriment. In Ellerth, the Court was presented with a claim framed in terms of *quid pro quo* harassment. However, the case more

closely resembled a hostile environment case, since the plaintiff had never submitted to the alleged harasser's demands, and therefore suffered no tangible job detriment.

Kimberly Ellerth alleged that a vice president of sales and marketing for Burlington Industries sexually harassed her throughout her employment by asking inappropriate questions, making lewd comments and sometimes touching her offensively. For example, he allegedly asked her whether she and her husband were practicing having a family while staring conspicuously at her breasts and legs, regaled her with off-color jokes; rubbed her leg under the table at a luncheon, made provocative comments about her breasts and legs and once suggested she perform fellatio. Ellerth also claims that her harasser reminded her that he could make her job "very hard or very easy at Burlington." She subsequently applied for and received a promotion, but claimed that the promotion decision was delayed by the harasser. Although Ellerth complained to various co-workers and various lower-level managers around her, she did not use Burlington's grievance procedure, or complain to her direct supervisor about the harassment.

The district court granted summary judgment to Burlington on Ellerth's *quid pro quo* claim on the grounds that Ellerth failed to demonstrate that she suffered any adverse employment action after rejecting her supervisor's advances. The Seventh Circuit reversed in a severely divided decision, which held that Burlington could be held liable for *quid pro quo* sexual harassment even though Ellerth could not show that she suffered any adverse job consequences. The court's decision ended with a plea to the Supreme Court to resolve "the chaotic case law in this important field of practice."

In its opinion, the Supreme Court downplayed the importance of the *quid pro quo* and *hostile environment* labels. Stating that it was not suggesting that the terms *quid pro quo* and hostile work environment are irrelevant to Title VII litigation, the court nevertheless made it clear in Ellerth that the *quid pro quo* label did not have any meaning in a case in which a harasser's threats of job detriment are not carried out. Where the harasser's threats are unfulfilled, the case should be analyzed under the hostile work environment paradigm, requiring a showing of severe or pervasive conduct. Ellerth, 524 U.S. at 753.

1. Required Elements of a Quid Pro Quo Claim

The traditional elements of a *quid pro quo* claim are as follows:

- (1) the employee is a member of a protected class;
- (2) the employee was subjected to unwelcome sexual harassment by supervisory or higher level personnel, in the form of sexual advances or requests for sexual favors;
- (3) the harassment complained of was based on sex;
- (4) the employee's submission to the unwelcome advances was made an express or implied condition for receiving job benefits *or* the employee's refusal to submit to a supervisor's sexual demands resulted in a tangible job detriment;

- (5) the existence of *respondeat superior* liability.

Highlander v. KFC Nat'l Management Co., 805 F.2d 644 (6th Cir. 1986).

As noted above, due to recent changes in the law of harassment, unfulfilled threats of adverse employment action must be analyzed under the hostile work environment “severe or pervasive conduct” paradigm, and additionally, employers are now vicariously liable for harassment committed by supervisors and managers. Accordingly, the authors will suggest that this *prima facie* model may no longer be accurate post-Ellerth. Based on the holding in Ellerth, in order to state a *quid pro quo* claim where the supervisor’s threats were unfulfilled, the fourth element might more appropriately read:

- (4) The employee’s submission to the unwelcome advances was made an express or implied condition for receiving job benefits *and* the employee’s refusal to submit to a supervisor’s sexual demands resulted in a tangible job detriment.

The fifth element should probably be deleted entirely in such situations, since under Ellerth, employers are vicariously liable for harassment committed by supervisors and managers and, if tangible job detriment results, the affirmative defense is not available. Thus, where an employee’s refusal to submit to a supervisor’s sexual demands results in a tangible job detriment, the traditional strict liability standard for employers remains intact.

What is unclear, following Ellerth, is the effect of the court’s decision on the traditional *quid pro quo* claim where the supervisor’s threat is not carried out because the employee has *submitted* to the supervisor’s unwelcome advances. As the Ellerth court noted, with reference to its earlier decision in Meritor:

We assumed, and with adequate reason, that if an employer demanded sexual favors from an employee in return for a job benefit, discrimination with respect to terms or conditions of employment was explicit. . . . We distinguished between *quid pro quo* claims and hostile environment claims, and said both were cognizable under Title VII, though the latter requires harassment that is severe or pervasive. The principal significance of the distinction is to instruct that Title VII is violated by either explicit or constructive alterations in the terms or conditions of employment and to explain the latter must be severe or pervasive.

Ellerth, 524 U.S. at 752 (citations omitted), citing Meritor, 477 U.S. at 72.

This suggests, at least, that the traditional *quid pro quo* paradigm may still be available to a plaintiff who has submitted to a supervisor’s unwanted advances, because her submission to the employer’s demands in exchange for a job benefit, or in order to keep a job benefit, constitutes an *explicit* alteration in the terms and conditions of her employment. If this is the case, then the only

effect of Ellerth on this type of *quid pro quo* claim may be to require reading the fifth prong of the Highlander test to provide for the availability of the affirmative defense in cases where the alteration of the victim's terms and conditions of employment fell short of constituting a "tangible employment action." For a discussion of what constitutes a "tangible employment action" see § [7.44], *infra*.

a. A Request for Sexual Favors Was Made

The request for sexual favors in exchange for a tangible job benefit must be either overt, or of such a nature that the sexual overture is clear. For example, in Perkovich v. Roadway Express, Inc., 106 F.3d 401 (6th Cir. 1997), the court found that *quid pro quo* conduct was not actionable where there was no overt request for sexual favors, and the plaintiff could only argue that the ordinary language used by the supervisor had a hidden sexual meaning. In addition, the court stated that a plaintiff's super-sensitivity was not sufficient to create a prima facie case.

The courts will not generally find sexual favoritism to be actionable unless the plaintiff can show: (1) that she was approached and rejected sexual advances, and then others who were receptive to sexual advances were given advantages she did not receive, or (2) favoritism toward sexual partners was so pervasive in the workplace that it became an implicit condition for receiving benefits or advancement. Isolated instances where sexual partners are favored do not give rise to actionable claims for *quid pro quo* sexual harassment, because both male and female employees who are not involved with the supervisor are at an equal disadvantage.

In Karibian v. Columbia University, 930 F. Supp. 134 (S.D.N.Y. 1996), a romantic relationship between a plaintiff and her supervisor soured. The plaintiff later sued her employer, claiming it had failed to take appropriate actions to deal with the supervisor's continued attraction to her after she made a complaint regarding his attentions. The court rejected her *quid pro quo* claims, finding that the earlier relationship was consensual, and no requests for sexual favors in exchange for a job benefit occurred after it ended. In this case, the evidence suggested only that there was a relationship that the plaintiff did not want any more. Accordingly, the court found that the employer had done enough when it transferred the plaintiff to another supervisor.

In Piech v. Arthur Andersen & Co., 841 F. Supp. 825 (N.D. Ill. 1994), the court ruled that the mere showing of preferential treatment and promotion given to female co-worker who was romantically involved with her supervisor would not be sufficient to state a cause of action for discrimination "based on sex," because all other eligible employees, male and female, who were not sexually involved with the supervisor did not receive a promotion. However, allegations that it was generally necessary for women to grant sexual favors to the employer's decision makers in order to obtain professional advancement, and that she was not extended certain employment benefits including promotion because unlike favored co-employees, she did not grant sexual favors, would be sufficient to state a cause of action for *quid pro quo* sexual harassment under Title VII.

b. The Request for Sexual Favors Was Unwelcome

The existence of a prior sexual relationship between a supervisor and an employee does not mean that later requests for sexual favors by the supervisor will be considered welcome. In Babcock

v. Frank, 729 F. Supp. 279 (S.D.N.Y. 1990), the plaintiff established a prima facie case of *quid pro quo* harassment where she demonstrated that although she had a prior consensual relationship with the supervisor, she later objected to his advances, and was then told by her supervisor she would be fired if she continued to refuse to sleep with him. Under these circumstances, the court found that the later advances could not be considered “welcome.”

c. The Request Was Coupled with a Threat

Where the employee rejects the sexual advances and has been threatened with an adverse employment consequence, the content of the threat must be sufficiently severe to affect the employee’s “compensation, terms, conditions, or privileges of employment.” Robinson v. City of Pittsburgh, 120 F.3d 1286, 1298 (3rd Cir. 1997). Thus, “[f]ormal reprimands that result in a notation in an employee’s personnel file could be sufficiently concrete, but harsh words that lack real consequences are not.” *Id.* In addition to termination, under prior law, the following actions were sufficient to be considered “adverse employment actions”:

- (1) denial of promotion; Robinson, 120 F.3d at 1298-99; Spencer v. Gen. Elec. Co., 894 F.2d 651 at 659 (4th Cir. 1990).
- (2) decrease in pay; Spencer, 894 F.2d at 659.
- (3) denial of participation in training program; Henson v. City of Dundee, 682 F.2d 897 (11th Cir. 1982).
- (4) reprimands; Horn v. Duke Homes, 755 F.2d 599 (7th Cir. 1985).
- (5) transfers; Katz v. Dole, 709 F.2d 251, 255 n.6 (4th Cir. 1983).
- (6) loss of job title; Bryson v. Chicago State Univ., 96 F.3d 912, 916 (7th Cir. 1996).
- (7) more rigid enforcement of leave policy. Gallagher v. Delaney, 139 F.3d 338 (2nd Cir. 1998).

2. Employer Liability for Supervisor Harassment

In Faragher v. City of Boca Raton, 524 U.S. 775 (1998), the United States Supreme Court was invited to consider whether the City of Boca Raton could be held strictly liable for hostile work environment sexual harassment by a supervisor. The plaintiff, Beth Anne Faragher, worked as a lifeguard for the City of Boca Raton. She alleged that between 1990 and 1995, two male supervisors touched and/or patted her thighs and buttocks on approximately 15-30 occasions and subjected her to a large number of extraordinarily offensive comments and gestures, including requests for oral sex and demands to join her in the lifeguard shower room.

Although Faragher did not formally report this conduct to the city during her employment, she did informally consult with Robert Gordon, whom she regarded as her friend and who also happened to supervise one of the harassers. Gordon did not speak to either man about the

harassment, or inform higher management of his discussion with Faragher. She later resigned as a lifeguard in order to attend law school, and then filed suit for sexual harassment.

The district court entered judgment for Faragher on her Title VII claim against the city, and awarded her \$1 in nominal damages. The Eleventh Circuit reversed, holding that the city could not be held liable because the supervisors did not act within the scope of their employment when they harassed Faragher, and there was no evidence that the supervisors were aided in the perpetration of their sexual harassment by any relationship with the city, since they did not make any adverse employment decisions based on Faragher's response to their sexual overtures.

In her petition for certiorari, Faragher argued that constructive knowledge should be imputed to an employer any time harassment is reported to an employee "whose job it reasonably should be to report the harassment up the line." In its amicus brief, the EEOC urged that the court should find that a harasser has been "aided in his harassment due to the existence of the agency relationship," whenever the victim reasonably fears adverse employment consequences if she resists the harasser's overtures or complains.

The Supreme Court determined that employers should be held vicariously liable for hostile work environment harassment carried out by supervisory employees, regardless of whether the employer had any actual or constructive notice of the harassment. However, as explained in § [7.41] below, where no tangible employment action has been taken against the plaintiff, employers may be able to take advantage of an affirmative defense to liability.

Faragher arose in the context of a hostile work environment case. As stated above, prior to the Supreme Court's decision in Ellerth, the distinction between hostile environment and *quid pro quo* sexual harassment was fundamentally important to the issue of employer liability. Employers had generally been held to be "strictly liable" for *quid pro quo* harassment on the part of their supervisors and managers. In Ellerth, the Supreme Court essentially recognized that the real distinction for employer liability purposes should not be between *quid pro quo* and hostile environment cases, but rather between cases in which the plaintiff suffered tangible job detriment and those in which she did not. Ellerth, 524 U.S. at 753. This distinction has since been recognized in the Sixth Circuit. Williams v. General Motors Corp., 187 F.3d 553 (6th Cir. 1999). Thus, where the threat of adverse job consequences in a traditional *quid pro quo* case goes unfulfilled (because the plaintiff called the supervisor's bluff, for example), the case will be analyzed as a hostile work environment case, requiring a showing of severe or pervasive conduct. On the other hand, where the threat has been fulfilled, resulting in "tangible" employment action such as discharge, demotion, decreased pay, etc. the employee will continue to be "strictly" liable and unable to utilize the affirmative defense discussed below.

3. Affirmative Defense Created Where Supervisor's Actions Did Not Result in Adverse Employment Action

The Supreme Court in Faragher and Ellerth also chose to create an affirmative defense that may relieve an employer from liability for a supervisor's actions. The availability of this defense depends upon whether the supervisor has taken some "tangible employment action" with respect to the employee during the course of the harassment. The affirmative defense requires that the employer show:

- 1) that it exercised reasonable care to prevent and correct promptly any sexually harassing behavior; and
- 2) that the employee unreasonably failed to take advantage of any preventive or corrective opportunities provided or to avoid harm otherwise.

However, as emphasized by the court, the affirmative defense is not available when the supervisor's harassment has culminated in a tangible employment action, such as discharge, demotion, or undesirable reassignment. *Id.* at 2293.

4. Issues Raised by the Affirmative Defense

Federal Circuit and District courts, and state courts throughout the country have embraced the Faragher and Ellerth affirmative defense and tackled some of the lingering questions left by the Supreme Court as to its interpretation. In addition, on June 18, 1999, the Equal Employment Opportunity Commission issued EEOC Enforcement Guidance: Vicarious Employer Liability of Unlawful Harassment by Supervisors ("Enforcement Guidance"). Some of the provisions of the Enforcement Guidance, and some cases construing the affirmative defense, are set forth below.

a. Who is a "Supervisor"?

Both Ellerth and Faragher announced that an employer may be vicariously liable for harassment by "a supervisor with immediate (or successively higher) authority over an employee." Under the Enforcement Guidance, an individual will qualify as an employee's "supervisor" if at least one of the following conditions is met:

- (1) the individual has the authority to undertake or recommend tangible employment actions affecting the employee;
- (2) the individual has the ability to direct the daily work activities of the employee; or
- (3) the employee reasonably believes the individual has supervisory power.

The ability to undertake or recommend tangible employment actions does not need to be absolute. The individual can be a supervisor even if he or she lacks the final say concerning employment decisions, or if the individual's decision is subject to approval by a higher authority. An

individual's ability to recommend tangible employment actions is sufficient if the recommendation "is given substantial weight by the final decision maker(s)."

With regard to the second condition, the EEOC states that it is recognized because "an individual's ability to commit harassment is enhanced by his or her authority to increase the employee's workload or assign undesirable tasks." This will apply even in cases where the authorization is only for a temporary or short-term basis. However, it will not apply when the individual directing work is in fact only relaying the work assignments determined by another employee, or where the individual has only limited authority to assign a small number of minor tasks.

Finally, an employee may reasonably believe an individual has actual supervisory authority in situations where the chain of command is unclear. This belief may also arise in situations where the employee knows the individual is outside the employee's chain of command, but has such a broad grant of authority over other matters, that the employee reasonably believes this authority provides the ability to influence the employee's working conditions.

b. What is a "Tangible Employment Action"?

Under the Enforcement Guidance, a "tangible employment action" has the following characteristics:

- (1) it requires an official act of the enterprise;
- (2) it usually is documented in official company records;
- (3) it may be subject to review by higher level supervisors; and
- (4) it often requires the formal approval of the enterprise and use of its internal processes.

Additionally, a tangible employment action usually results in economic harm to the employee, and is an act that could only be carried out by an individual who has the power to act with the authority of the company.

Examples of tangible employment actions include:

- (1) hiring and firing;
- (2) promotion and failure to promote;
- (3) demotion;
- (4) undesirable reassignment;
- (5) a decision resulting in a significant change in benefits;

- (6) compensation decisions; and
- (7) work assignment.

An employment decision is not “tangible” if it only results in an insignificant change in the employee’s status. For example, transferring an employee to a new job with only slightly different responsibilities, with no change in pay or benefits would generally not qualify. However, if the new job constitutes a demotion, or places the employee in a position with reduced promotional opportunities, a tangible employment action may be found.

An employee must always demonstrate that any “tangible employment action” imposed by the supervisor was causally connected to the harassment carried out by the supervisor, *i.e.*, a subsequent demotion occurred *because* the employee rejected the employer’s sexual advances. However, the EEOC takes the position that “[a] strong inference of discrimination will arise whenever a harassing supervisor undertakes or has significant input into a tangible employment action affecting the victim, because it can be assumed that the harasser could not act as an objective, non-discriminatory decision maker with respect to the [employee].” If the employer provides a legitimate, non-discriminatory reason for the employment action, then the employee must show that the offered reason is a pretext for discrimination. Unless the employee meets this burden, the affirmative defense is still available to the employer.

c. What if Only One Prong of the Affirmative Defense Can Be Met?

Where a supervisory employee has created a hostile work environment, or has engaged in *quid pro quo* harassment, but no “tangible employment action” has yet occurred, the employer has the ability to avoid vicarious liability by showing:

- (1) it exercised reasonable care to prevent and promptly correct any harassment; and
- (2) the employee unreasonably failed to take advantage of any preventive or corrective opportunities provided by the employer or to avoid harm otherwise.

The Enforcement Guidance notes that this standard will only operate to relieve the employer of liability if both of the above requirements are met. “If an employer cannot prove that it discharged its duty of reasonable care *and* that the employee unreasonably failed to avoid harm, the employer will be liable.” However the Enforcement Guidance expresses the opinion that in most hostile work environment cases, if both of these events occur, harassing conduct can be stopped before it rises to the level of actionable harassment, which would also allow the employer to escape any liability for the supervisor’s conduct. ‘An effective complaint procedure “encourages employees to report harassing conduct before it becomes severe or pervasive” and if an employee promptly utilizes that procedure, the employer can usually stop the harassment before actionable harm occurs.’ This would only fail to provide relief if the conduct that created the hostile work environment was so severe that it rose to the level of actionable harassment almost immediately.

d. The Employer's Duty of Reasonable Care

The employer's duty of care will be satisfied where it establishes, disseminates and enforces an anti-harassment policy and complaint procedure, and takes other reasonable steps to prevent and correct harassment. Although noting that they are not mandatory, the Enforcement Guidance recommends that an anti-harassment policy contain the following provisions:

- (1) prohibition of harassment;
- (2) protection against retaliation;
- (3) a clearly described complaint process, with more than one avenue for making complaints;
- (4) an assurance that any report will be treated confidentially to the extent possible;
- (5) a complaint process that provides for prompt, thorough, and impartial investigation of complaints; and
- (6) an assurance that immediate and appropriate action will be taken if the employer determines that harassment has occurred.

In this regard, practitioners in Kentucky should be aware of the Kentucky Supreme Court's decision in Bank One, Kentucky, N.A. v. Murphy, 52 S.W.3d 540 (Ky. 2001). In this case, the plaintiff, Ms. Murphy, apparently endured a series of sexually harassing acts by her supervisor, Grant. She reported this to her previous (female) supervisor, Korphage, who told Murphy she too had experienced harassment from the same individual. Murphy reported the harassment to Bank One's HR Department, which conducted an apparently thorough investigation, resulting in the supervisor's resignation. Nevertheless, Murphy sued, alleging sexual harassment. The Bank defended on the basis of the Faragher/Ellerth affirmative defense. Murphy contended that the "reasonable care" prong of the affirmative defense could not be met, however. Despite the fact that the Bank apparently had a sufficient sexual harassment policy and had promptly taken steps to correct the harassment alleged by Murphy, Murphy took the position that the Bank had failed to take appropriate action when Korphage had previously reported Grant's actions. Even though the facts show that Korphage had refused to file a formal complaint, stating that she wished to remain anonymous, and refused to cooperate in an investigation, the Court noted that Grant's deposition testimony revealed that he had never been confronted with the facts of the Korphage incident by name. Because it was unclear from the record whether the investigation into the Korphage incident was complete, the Supreme Court remanded the matter to the trial court for a factual determination. This case demonstrates that Kentucky courts have embraced the concept of the affirmative defense set forth in Faragher and Ellerth. However it also shows that Kentucky employers must be certain that *every* complaint of harassment is carefully investigated, even though the complainant may wish to remain anonymous or refuse to participate. Failure to do so may negatively affect the employer's ability to use the affirmative defense in future cases unrelated to the one at issue.

e. The Employee's Obligation to Avoid Harm

The Enforcement Guidance provides that "an employer who has exercised reasonable care... is not liable for unlawful harassment if the aggrieved employee could have avoided all of the actionable harm." Likewise, "[i]f some but not all of the harm could have been avoided, then an award of damages will be mitigated accordingly."

This generally means that the employee must use the employer's complaint procedure to try to resolve the harassment. Further, the employee should use the procedure in good faith, by providing complete information to the employer, and cooperating with the employer's investigation. Additionally, the employee should make a complaint as soon as possible after objectionable conduct has occurred. If the employee fails to take these steps, the employer will have the opportunity to argue that the employee failed to take reasonable steps to avoid harm.

However, the Enforcement Guidance recognizes that in some cases, the employee will be relieved of the obligation to make a complaint of harassment. These may exist where the employee had reason to believe that:

- (1) making a complaint would result in retaliation;
- (2) there were obstacles in the procedure that actually discouraged complaints, such as burdensome or intimidating reporting requirements;
- (3) the complaint mechanism was ineffective.

The Enforcement Guidance also provides that even if the employee "unreasonably failed" to use the employer's complaint procedure, the employer may not be able to satisfy the second prong of the affirmative defense if the employee took "other efforts to avoid harm." Interestingly, one of the examples of other efforts to avoid harm includes making a complaint to the EEOC or its state equivalent. The other examples provided are filing a union grievance, or, in the case of an employee who was engaged through a temporary agency, making a complaint to the temporary agency. However, the guidance notes that the timing of the complaint to such a third party may affect liability or damages. For example, if the employee could have avoided some of the harm by making the complaint to the employer at an earlier time, then the damages that employee can recover will be limited accordingly.

Regardless of whether the courts would view a complaint to an outside agency as an acceptable alternative to using an employer's reasonable complaint procedure, employers who receive their first notice of a complaint when served with a charge of discrimination, or by some other outside source, should respond to the notification by immediately conducting a thorough investigation and taking any appropriate corrective action thereafter.

5. Vicarious Liability for the Actions of High Level Employees

Finally, the guidance provides that harassment by certain high level employees is the equivalent of harassment by the “employer.” Because these individuals are a “proxy” for the organization, their acts are imputed to the employer automatically, precluding the employer from raising the affirmative defense. Examples of those individuals include:

- (1) a president of a corporation;
- (2) the owner of a company;
- (3) a partner;
- (4) a corporate officer.

In October of 1999 the EEOC also revised its previously issued Sex Discrimination Guidelines and National Origin Guidelines, 60 Fed. Reg. 58,333 (1999), amending 29 CFR Parts 1604 and 1606, to revise its earlier statements on vicarious liability for harassment by a supervisor, in order to comply with Ellerth and Faragher.

IV. Harassment on the Basis of Other Protected Classifications

A. Additional Causes of Action for Harassment under Title VII

While causes of action for sexual, racial and gender based harassment are well known, it is important for employers to recognize that the hostile environment cause of action applies to all types of discrimination prohibited under Title VII. In light of the events of September 11, 2001, it is particularly timely to remember that employees are protected from harassment and discrimination on the basis of their religion and national origin. On September 14, 2001, Cari M. Dominguez, Chair of the EEOC, issued a press release urging employers and employees across the country to “promote tolerance and guard against unlawful workplace discrimination based on national origin or religion.”

1. National Origin Harassment

An employer has an affirmative duty to maintain a working environment free of harassment on the basis of national origin. 29 C.F.R. § 1606.8(a); *see* Appendix, Section [4.2], for the complete text of § 1606.8. National origin discrimination is not defined under Title VII; however, the EEOC has defined national origin discrimination as “including, but not limited to, the denial of equal employment opportunity because of an individual’s, or his or her ancestor’s, place of origin; or because an individual has the physical, cultural or linguistic characteristics of a national origin group.” 29 C.F.R. §1606.1.

Under the regulation:

Ethnic slurs and other verbal or physical conduct relating to an individual's national origin constitute harassment when this conduct:

- (1) has the purpose or effect of creating an intimidating, hostile, or offensive working environment,
- (2) has the purpose or effect of unreasonably interfering with an individual's work performance, or
- (3) otherwise adversely affects an individual's employment opportunities.

29 C.F.R. §1606.8(b).

In Boutros v. Canton Regional Transit Authority, 997 F.2d 198 (6th Cir. 1993), the Sixth Circuit held that to establish a *prima facie* case of a hostile work environment due to national origin under Title VII or Section 1983, a plaintiff must show the following:

- (1) he was a member of a protected class;
- (2) he was subjected to harassment based upon national origin;
- (3) the harassment unreasonably interfered with his work performance and created an intimidating, hostile, or offensive work environment; and
- (4) the existence of *respondeat superior* liability.

Id. at 203 (as modified by Harris v. Forklift Systems, Inc., 510 U.S. 17, 21-22 (1993) (offensive conduct does not need to be psychologically injurious).

The plaintiff in this case presented evidence that throughout his employment he was subjected to numerous disparaging ethnic stereotypical epithets, such as "camel jockey" or "camel rider" made in demeaning reference to his Arab ancestry, either by or with the knowledge of his supervisors. Overturning the lower court's grant of directed verdict for the employer, the Court found that this evidence was sufficient to send his claim for hostile environment harassment to a jury. See also Miller v. Kenworth of Dothan, Inc., 277 F.3d 1269 (11th Cir. 2002) (Allegations that hispanic employee was subjected to ethnic slurs and derogatory nicknames on a daily basis over a one-month period and that his co-workers used these slurs and derogatory names in an intimidating manner to berate and taunt employee demonstrated conduct that rose above the level of off-handed comments or casual conversation. Taken in the light most favorable to the plaintiff, these allegations were sufficient to allow a reasonable jury to find that the employee was subjected to severe and pervasive harassment that was sufficient to alter the terms or conditions of his employment.); Erebia v. Chrysler Plastics Products Corp., 772 F.2d 1250 (6th Cir. 1985) (In a Section 1981 action against

employer for maintaining hostile work environment, evidence that plaintiff was subjected to racial slurs by hourly employees and that he reported slurs regularly to three different managers who at best did nothing in response or at worst threatened him economic harm was sufficient to support jury's verdict for plaintiff.); *but see Flores v. J.C.Penny Co., Inc.*, 2002 WL 397669 (D. Kan. Mar. 8, 2002) (Summary judgment for employer upheld. In order to show harassment based on national origin, the plaintiff must present more than just a subjective belief that the harsh comments made repeatedly to her by her supervisor which did not mention or refer to her ethnicity were actually motivated by her national origin.).

2. Religious Harassment

Title VII's treatment of religion is somewhat unique. This is based in part on the constitutional requirements of separation of church and state. Title VII prohibits discrimination on the basis of religion, but it provides an exemption for religious institutions that discriminate on the basis of religious affiliation. Also, under Title VII, religious discrimination can take two seemingly opposite forms: (1) discrimination that arises when an employee is treated differently because of his or her religious faith or affiliation, and (2) discrimination that occurs when an employer fails to reasonably accommodate an employee's religious observances and practices.

There is no bright-line test available to determine what qualifies as a "religion" or "religious belief," and what does not. "Religion" is defined by the EEOC at 29 C.F.R. § 1605.1, which provides in part:

[T]he Commission will define religious practices to include moral or ethical beliefs as to what is right and wrong which are sincerely held with the strength of traditional religious views. . . . The fact that no religious group espouses such beliefs or the fact that the religious group to which the individual professes to belong may not accept such belief will not determine whether the belief is a religious belief of the employee or prospective employee. The phrase "religious practice" as used in these Guidelines includes both religious observances and practices, as stated in Section 701(j), 42 U.S.C. 2000e(j).

Courts have relied on similar definitions of religion that have evolved in First Amendment litigation. *Frazee v. Illinois Dep't of Employment Sec.*, 489 U.S. 829 (1989). A "religion" does not require a God or deity or even a written theology, but to be a "religion" the ideology must be more than a political, economic or social philosophy. In *Frazee*, the Supreme Court explained:

There is no doubt that "only beliefs rooted in religion are protected by the Free Exercise Clause." Purely secular views do not suffice. Nor do we underestimate the difficulty of distinguishing between religious and secular convictions and in determining whether a professed belief is sincerely held.

Id. at 833.

Title VII prohibits harassment on the basis of religion, using the same framework for proving harassment on the basis of sex, race, or national origin. To prevail on a religious harassment claim, the plaintiff must show that the conduct was pervasive, that it was unwelcome and offensive, and that it was directed at the plaintiff due to his or her religious beliefs or practices. For example, in Weiss v. U.S., 595 F. Supp. 1050 (E.D. Va. 1984), the court found that an occasional offensive religious epithet by a co-worker does not necessarily give rise to a Title VII claim against an employer. However, when an employee is repeatedly subjected to demeaning and offensive religious slurs over a two year period by a co-worker and by his supervisor, including such taunts as “resident Jew,” “Jew faggot,” “rich Jew,” “Christ killer,” “nail him to the cross,” and “you killed Christ, Wally, so you’ll have to hang from the cross.” it would have the effect of altering the conditions of his employment within the meaning of Title VII. *Id.* at 1056 (citing Compston v. Borden, Inc., 424 F. Supp. 157, 160-61 (S.D. Ohio 1976) (when a person vested with managerial responsibilities embarks upon a course of conduct calculated to demean an employee before his fellows because of the employee’s professed religious views, such activity will necessarily have the effect of altering the conditions of his employment)).

The harassment is not required to be religious in content, only motivated by the plaintiff’s religion. In Turner v. Barr, 811 F. Supp. 1 (D.D.C. 1993), the plaintiff alleged both racial and religious harassment. He was able to show that he was subjected to jokes about the Holocaust by one of his supervisors and that he and other white and Jewish employees were placed in segregated seating areas, not permitted to work overtime in amounts comparable to other non-white and non-Jewish employees, and a poster referring to the plaintiff with a derogatory nickname, although non-racial and non-religious, was placed in the workplace. The defendant claimed that the case for religious harassment was insufficient because only a few incidents of alleged harassment had any religious content. Relying on its prior opinion in McKinney v. Dole, 765 F.2d 1129 (D.C. Cir. 1985), the court found the evidence was sufficient to sustain the plaintiff’s claim, as “evidence of harassment need not have explicitly racial or religious overtones. The Plaintiff need only show that the harassment would not have occurred but for the Plaintiff’s race or religion.” Turner, 811 F. Supp. at 4. The court found that when viewing the “totality of the circumstances,” both the frequency of the events and their severity justified a finding that the plaintiff was subject to harassment on the basis of his race and religion. *Id.* at 5.

However, the courts have recognized that unlike an employee’s race, gender, or national origin, an employee’s religious beliefs may conflict with legitimate job-related demands made by the employer. When this happens, the employer’s demands should not be confused with religious harassment. In Beasley v. Health Care Serv. Corp., 940 F.2d 1085 (7th Cir. 1991), the court clarified the level of personal commitment to work that a company can expect from employees without creating religious harassment. In this case, the employer did not engage in religious harassment when the employer told its employees during a training session that their jobs should be the “first priority” in their lives. The plaintiff in this case stated that since, according to her religious beliefs, God was her first priority, having this type of requirement for employees constituted religious harassment. The court found that, in the absence of any actual impact this expectation had on her practice of religion, the company could continue to use such language and request that its employees

make their jobs top priority in their lives. This demonstrates the additional twist to analyzing harassment claims that is created by the requirement that an employer make a reasonable accommodation for an employee's religious beliefs.

Similarly, in Hoffman v. Lincoln Life and Annuity Distributors, Inc., 174 F. Supp. 2d 367 (D. Md. 2001), the employee's religious harassment claim failed, as she presented no evidence that she ever informed her employer that any employment requirements of her job conflicted with her religious beliefs. Although she stated that she objected to the sexual jokes she had viewed while screening her supervisor's e-mail, she did not inform her supervisor that this objection was based on religious grounds. There was only one occasion when she was asked to perform a task to which she raised a religious objection (mailing a flier to an organization of gay and lesbian professionals, to which the company had marketed itself and received business), and after she explained that this offended her religious beliefs, she was not required to assist any further with this mailing.

V. The Emergence of Causes of Action for Harassment Under Other Anti-Discrimination Laws:

A. The Age Discrimination in Employment Act

The Age Discrimination in Employment Act ("ADEA"), 29 U.S.C. § 621 *et. seq.*, prohibits discrimination in the compensation, terms and conditions of employment on the basis of age. 29 U.S.C. § 623(a)(1). It protects individuals who are age 40 and over. 29 U.S.C. § 631(a). Remedies available under the ADEA are similar to those provided by Title VII, and include backpay, front pay, and attorney fees. Although compensatory and punitive damages are not available under the ADEA, the courts may elect to provide liquidated damages in an amount not to exceed backpay for willful violations of the ADEA. 29 U.S.C. § 626(b). In addition, the courts have the ability to provide equitable relief and may order that the plaintiff be hired, promoted, transferred, or receive some other job benefit that was unlawfully denied on the basis of age. The ADEA contains enforcement provisions similar to those found in Title VII, and it requires the filing of an administrative charge with the EEOC or a state or local human right agency prior to the filing of a state or federal court action. 29 U.S.C. § 633(b).

B. The Americans with Disabilities Act

Title I of the Americans with Disabilities Act ("ADA"), 42 U.S.C. § 12111 *et. seq.*, prohibits employers from discriminating against "qualified individuals with disabilities" in the terms, conditions and privileges of employment, including their job application procedures and hiring, advancement and discharge practices. 42 U.S.C. 12112(a). In addition to prohibiting discrimination, the ADA also places an affirmative burden on employers to provide a reasonable accommodation to an individual with a disability, if such accommodation will allow the individual to: (1) perform the essential functions of his or her position, or (2) otherwise participate in a process designed to evaluate applicants for employment or evaluate current employees for compensation and advancement purposes. 42 U.S.C. § 12111(9).

The ADA's enforcement provisions are similar to those found in Title VII, and they require an individual to file a charge of discrimination with the EEOC prior to filing a lawsuit in state or federal court. The remedies provided under the ADA are basically the same as those provided under Title VII, with one exception. A successful ADA plaintiff may receive back pay, front pay, injunctive relief, attorney fees, and compensatory and punitive damages. However, in cases where the violation complained of is the employer's failure to provide a reasonable accommodation, the employer can avoid liability for compensatory and punitive damages if it demonstrates that it made good faith efforts to provide such an accommodation.

C. Employer Liability for Age and Disability Based Harassment

Because these two anti-discrimination laws are so similar to Title VII, it is not surprising that the courts have now begun to recognize that the ADEA and ADA also provide causes of action for harassment on the basis of age and disability.

1. Cases Discussing Age-Based Harassment

The Sixth Circuit, in Crawford v. Medina General Hospital, 96 F.3d 830 (6th Cir. 1996), held that this similarity required the recognition of a cause of action under the ADEA for age-based harassment. The court held that a claim for hostile work environment under the ADEA could be established by showing that:

- (1) the plaintiff was at least forty years old;
- (2) the plaintiff was harassed based on his or her age;
- (3) the harassment had the effect of unreasonably interfering with the plaintiff's work, by creating an environment that was both objectively and subjectively hostile or offensive; and
- (4) the plaintiff has some basis for imputing liability to the employer.

Id. at 834-35.

In Crawford, the plaintiff alleged that her co-workers mistreated her and were rude to her because of her age. She presented evidence that she was excluded from parties outside the office, that a supervisor commented that she did not think "women over 55 should be working," and that "old people should be seen and not heard." Using the above standard, the court found that although age-based harassment was actionable under the ADEA, the plaintiff had failed to establish a *prima facie* case:

Unquestionably, there was hostility and abusiveness in this working environment, but the evidence suggests that the atmosphere stemmed from a simple clash of personalities. In any event, there is an absence of evidence that it stemmed from a dislike of people over a particular

age. . . . [I]mportantly, it is Crawford who simply assumes, without objectively articulable support, that when she was insulted with age-neutral insults, it was *because of her age*.

Along those same lines, we think it is patent that we must entirely discount the plaintiff's complaints insofar as they focus on coworkers having parties without inviting her, or coworkers being surly or impolite. Even if coworkers failed to invite her to parties *because* she was over 55, it seems obvious that the ADEA was not intended to remedy minor social slights and the resulting hurt feelings. Pizza parties are simply not a term, condition, or privilege of employment of which Congress has taken cognizance. . . . Similarly, while a supervisor's opinion that women should retire at age 55 may be unenlightened and logically indefensible, and might be circumstantial evidence of age discrimination if the supervisor were later to have fired Crawford, it hardly rises even to the level of an "offensive utterance," as it is simply one person's opinion, susceptible to retort and dispute. . . . Crawford has not produced any evidence tending to show that the harassment interfered with her work performance and/or created an objectively intimidating, hostile, or offensive work environment, within the meaning of [*Harris v. Forklift Systems, Inc.*, 510 U.S. 17 (1993)]. We note there is absolutely no suggestion that the environment impeded Crawford's work performance; indeed, she herself claims to like her job, despite [her supervisor's] asserted abusiveness.

Id. at 836; *see also* *Brennan v. Metropolitan Opera Ass'n, Inc.*, 192 F.3d 310 (2nd Cir. 1999) (*citing Crawford*) (summary judgment in favor of the employer on age-based harassment claim upheld where there was no evidence that the alleged harasser knew plaintiff's age and the three instances of hostility recounted by plaintiff had nothing to do with age, and even if they had been motivated by age, they would be insufficient as a matter of law to demonstrate a hostile work environment); *Causey v. Balog*, 162 F.3d 795 (4th Cir. 1998) (Federal district court properly dismissed claims of racial and age-based harassment by former city employee who alleged that supervisor interfered with his ability to complete projects, limited his access to supervisor, withheld information, refused to allow him to attend some job-related seminars on job time, imposed unreasonable deadlines, reassigned tasks to subordinates, ignored his advice, and chastised him, despite former employee's conclusory statements that supervisor treated him less favorably than younger black and white employees of similar rank, since he presented no evidence suggesting that supervisor's conduct was motivated by his age or race, supervisor never made any derogatory comments about his race or age, and nothing about supervisor's conduct suggests that it was based on these factors.); *but see* *Woodford v. Community Action Agency*, 239 F.3d 517 (2nd Cir. 2001) (Plaintiff offered sufficient evidence in her complaint of harassment on basis of her age to overcome employer's motion to dismiss where she attached exhibit stating her birth date to show that she was of protected age and she alleged that supervisor repeatedly and explicitly stated that she was too old to remain in her position, that he harassed her in attempt to force her to resign, that she filed internal grievances

complaining of his conduct, and that he retaliated against her by, among other things, discharging her.).

2. Cases Discussing Disability-Based Harassment

In 2001, the Fifth Circuit became the first United States Court of Appeals to recognize a cause of action under the ADA for hostile work environment harassment. In Flowers v. Southern Regional Physician Services, Inc., 247 F.3d 229 (5th Cir. 2001), the plaintiff, a medical assistant, filed a complaint of harassment and unlawful termination by her supervisors based on her HIV-positive status. She alleged that after learning of her disability, her immediate supervisor engaged in conduct such as intercepting her telephone calls, eavesdropping on her conversations, and hovering around her desk. Despite paying more attention to her on the job, he also stopped socializing with her outside the workplace. Other supervisory employees also avoided contact with her and refused to shake hands with her. In addition, she was selected for four “random” drug tests within a one-week period and was written up for poor performance and placed on probation twice, despite receiving high performance appraisals by her supervisors before they knew of her HIV-positive status.

The trial court allowed the plaintiff’s harassment claim to proceed to a jury, where she received a favorable verdict. The employer then appealed the jury’s verdict for the plaintiff, asking the appellate court to reject this theory of liability under the ADA. The Fifth Circuit rejected the employer’s argument, finding that the ADA’s prohibition against discrimination on the basis of disability in the terms and conditions of employment must be read to provide the same causes of action the Supreme Court has recognized as existing under Title VII:

We conclude that the language of Title VII and the ADA dictates a consistent reading of the two statutes. Therefore, following the Supreme Court’s interpretation of the language contained in Title VII, we interpret the phrase “terms, conditions, and privileges of employment,” as it is used in the ADA, to “strike at” harassment in the workplace.

Id. at 233 (citing Meritor Savings Bank v. Vinson, 477 U.S. 57, 64 (1986)). In further support of its position, the Fifth Circuit also acknowledged that the Sixth Circuit, in Keever v. Middletown, 145 F.3d 809, 813 (6th Cir. 1998), had previously recognized that the ADA would support a cause of action for hostile work environment, although the Keever court had provided no analysis in support of this position.

Less than two weeks later, the Fourth Circuit, in Fox v. General Motors, 247 F.3d 169 (4th Cir. 2001), used identical logic to recognize that a cause of action for disability-based harassment exists under the ADA. In this case, the plaintiff alleged that after returning to work following a back injury, his supervisors and co-workers regularly insulted him, made fun of his disability, withheld work-related materials from him, instructed other employees to avoid him, and gave him work assignments beyond his limitations that aggravated his back injury. As in Flowers, the employer in this case was also unsuccessfully appealing a jury verdict in the plaintiff’s favor.

VI. Individual Liability For Workplace Harassment

A. Liability Under Title VII

Title VII imposes liability upon “employers,” employment agencies, labor organizations and joint labor-management committees. 42 U.S.C. § 2000e(a)-(d). An employer is defined as:

[A] person engaged in an industry affecting commerce who has fifteen or more employees and any agent of such a person.

42 U.S.C. § 2000e(b). Prior to 1993, most courts interpreted this definition to impose individual liability on supervisors for their harassing conduct where they were acting as “agents of an employer” or “within the scope of their employment.” The Ninth Circuit was the first circuit to reject individual liability under Title VII, in Miller v. Maxwell’s International, 991 F.2d 583 (9th Cir. 1993). The Miller court considered the legislative intent expressed in the Civil Rights Act of 1964 and noted that Congress had limited liability under Title VII to employers with 15 or more employees in order to spare smaller employers the cost of litigating discrimination claims. Because Congress decided to protect small entities with limited resources from liability, the Ninth Circuit court found that it was inconceivable that it intended to allow civil liability to run against individual employees. *Id.* at 587.

The United States District Courts of both the Eastern and Western Districts of Kentucky as well as the Sixth Circuit Court of Appeals have ruled there is no individual liability under Title VII. In Lowry v. Clark, 843 F. Supp. 228 (E.D. Ky. 1994), the Eastern District of Kentucky expanded Miller’s reasoning by taking into consideration the changes to Title VII embodied in the Civil Rights Act of 1991. Noting that the 1991 Act imposed damage caps upon employers based on the number of persons they employ, it reasoned that Congress did not intend to permit recovery against individual employees for these damages. The Western District of Kentucky followed suit shortly thereafter in Winston v. Hardee’s Food Sys., Inc., 903 F. Supp. 1151, 1155 (W.D. Ky. 1995).

In 1997, the Sixth Circuit Court of Appeals endorsed the position of the Miller court and Kentucky’s federal district courts by holding that individual employees and supervisors, who do not otherwise qualify as “employers,” can not be held personally liable under Title VII. Wathen v. General Electric Co., 115 F.3d 400, 405 (6th Cir. 1997).

Nearly all federal courts that have considered the issue of whether individual liability exists under Title VII have now ruled that it does not. Sheridan v. E.I. DuPont de Nemours and Co., 100 F.3d 1061 (3rd Cir. 1996), *cert. denied*, 521 U.S. 1129 (1997); Tomka v. Seiler Corp., 66 F.3d 1295 (2nd Cir. 1995); Gary v. Long, 59 F.3d 1391 (D.C. Cir.), *cert. denied*, 516 U.S. 1011 (1995); EEOC v. AIC Security Investigations Ltd., 55 F.3d 1276 (7th Cir. 1995), *reh. en banc denied* (1995) (ADA case); Lenhardt v. Basic Inst. of Tech., 55 F.3d 377 (8th Cir.) (construing state law), *reh. en banc denied* (1995); Smith v. Lomax, 45 F.3d 402 (11th Cir. 1995); Grant v. Lone Star Co., 21 F.3d 649 (5th Cir.), *cert. denied*, 513 U.S. 1015 (1994).

B. Individual Liability for Harassment Under the Kentucky Civil Rights Act

The Sixth Circuit has also interpreted the KCRA's provisions prohibiting discrimination by "employers" to preclude the imposition of individual liability on harassers. Wathen v. General Electric Co., 115 F.3d 400, 405 (6th Cir. 1997) (interpreting KRS 344.040).

C. Individual Liability for Retaliation Under the KCRA

However, in Morris v. Oldham County Fiscal Court, 201 F.3d 784, 794 (6th Cir. 2000), the Sixth Circuit held that individuals *may* be held liable under KRS Chapter 344 for retaliation. The Court explained that KRS Chapter 344 *generally* mirrors Title VII but that the two acts have very different retaliation provisions. Title VII forbids retaliation by "an employer," whereas KRS Chapter 344 forbids retaliation by "a person." *Id.*; *see also Stacy v. Shoney's Inc.*, 142 F.3d 436 1998 WL 165139 (6th Cir. 1998) (unpublished decision).

VII. Developments in the Procedural and Evidentiary Areas of Harassment Law

A. Exhaustion of Administrative Remedies and the Timely Filing Requirement

A civil complaint alleging violation of Title VII, the ADA, or the ADEA must be preceded by the timely filing of a charge of discrimination with the EEOC. Title VII further requires that the charge "be in writing under oath or affirmation." 42 U.S.C. § 2000e-5(b) (§ 706(b) of the Civil Rights Act of 1964). If these and other procedural requirements that exist in the administrative framework used to pursue Title VII, ADA, and ADEA claims are not met, both the prosecution of the charge and any civil litigation thereafter may be foreclosed.

1. Use of the Continuing Violation Rule to Expand the Time Period for Filing a Charge of Harassment.

To be timely, the EEOC charge must be filed within 180 days of an act of discrimination, unless the charge is filed in a timely manner with a state or local human rights agency. In such cases, the time to file the EEOC charge is generally expanded to 300 days from the time the discrimination occurred.

Because of this relatively short filing period, it is frequently the case that while one or more of a plaintiff's alleged incidents of harassment took place within the 180/300 day period, there are also other alleged acts that occurred prior to this time period. In order to bring claims based, at least in part, on acts occurring outside the 180/300 day window, the plaintiff may claim that the prior acts of harassment are part of a continuing violation by the employer and attempt to invoke the "continuing violation" rule. The plaintiff may do this in an attempt to seek recovery for all alleged acts of wrongdoing, or at a minimum, to allow for the introduction of evidence of the less recent acts in the hope that this will bolster the validity of the timely claims. These same considerations apply to plaintiffs filing under Kentucky law. However, because of the longer filing period, the situation is less common.

The Sixth Circuit has applied the continuing violation rule to allow the introduction of evidence about, and recovery for acts occurring, outside the 180/300 day limitations period in two narrowly limited instances. Bell v. Ohio State University, 2002 WL 193694 (S.D. Ohio, Feb 5, 2002). The first situation is where there are past violations plus current discriminatory activity of the same type, such as “where an employer continues to presently impose disparate work assignments or pay rates between similarly situated employee groups.” EEOC v. Penton Industrial Pub., 851 F.2d 835, 838 (6th Cir. 1988). This category requires a current and a continuing discriminatory act and cannot be based merely on the continuing ill-effects of a past violation. Tolbert v. State of Ohio Dep’t of Transportation, 172 F.3d 934, 940 (6th Cir. 1999); Dixon v. Anderson, 928 F.2d 212, 216 (6th Cir. 1991).

The second instance requires “a longstanding and demonstrable *policy* of discrimination.” Dixon, 928 F.2d at 216 (emphasis added). In general, repeated requests for further relief from a prior act of discrimination is insufficient; rather, there must be a continuing “overarching policy of discrimination.” Janikowski v. Bendix Corp., 823 F.2d 945, 948 (6th Cir. 1987). “Repeated requests for further relief from a prior act of discrimination will not set the time limitations running anew.” *Id.* at 949. However, where there has been a long-standing policy of discrimination, repeated attempts to gain employment or promotions may each trigger the running of a new limitations period. Roberts v. North American Rockwell Corp., 650 F.2d 823, 827 (6th Cir. 1981).

Other circuits have also applied the continuing violation rule narrowly when considering whether to allow the introduction of evidence of events occurring outside the administrative filing period. For example, in Van Zant v. KLM Royal Dutch Airlines, 80 F.3d 708 (2nd Cir. 1996), the plaintiff filed an EEOC complaint on August 4, 1992. However the majority of incidents about which the plaintiff complained occurred prior to September 5, 1991 (more than 300 days earlier). The court observed that the continuing violation theory would apply in only two instances: (i) where there is evidence of an ongoing discriminatory policy or practice, such as the use of discriminatory seniority lists or employment tests, and (ii) where specific and related instances of discrimination are permitted by the employer to continue unremedied for so long as to amount to a discriminatory policy or practice. The court refused to allow the plaintiff to invoke the continuing violation rule because the plaintiff’s evidence showed neither a connection between KLM’s treatment of her and any company policy or practice. Further, the evidence did not show that KLM allowed related incidents of discrimination to go unremedied for so long as to amount to a discriminatory policy or practice.

In West v. Philadelphia Elec. Co., 45 F.3d 744 (3rd Cir. 1995), the Third Circuit held that, in order to establish that a claim falls within the continuing violation rule, the plaintiff must first demonstrate that at least one act occurred *within* the filing period and then establish that the harassment complained of is “more than the occurrence of isolated or sporadic acts of intentional discrimination.” Thereafter, the court explained, if the continuing violation theory applies to the plaintiff’s claims, this causes the statute of limitations issue to drop out of a case, and the plaintiff may introduce evidence of events outside the statute of limitations. The plaintiff may offer evidence of, and recover for, the entire continuing violation.

In Koelsch v. Beltone Electronics Corp., 46 F.3d 705 (7th Cir. 1995), the Seventh Circuit found that, in order for the continuing violation rule to apply, the event(s) occurring within the 300 day period must be closely related to acts falling outside this window. In this case, the plaintiff first filed a charge of discrimination in April 1992, primarily based on incidents of sexual harassment that she claimed occurred in 1988 and 1990. In an attempt to maintain these older claims, she tried to link the prior acts to other alleged acts of harassment occurring within the statutory filing period. However, when the court examined the timely claims, it found that they were isolated and unrelated to the incidents that may have occurred in 1988 and 1990. Therefore, the court determined that the earlier incidents of harassment were time-barred.

However in Galloway v. General Motors Service Parts Operations, 78 F.3d 1164 (7th Cir. 1996), the Seventh Circuit did allow a plaintiff to bring a sexual harassment lawsuit based on conduct which occurred both within the 300 day filing period and prior thereto. In Galloway, the court found that the pre-filing period conduct the plaintiff alleged was not the sort of conduct which would reasonably cause an employee to file suit (constituting, as the court found, single, isolated comments). The court opined that a plaintiff may base his or her suit on conduct that occurred outside the statute of limitations if it would have been unreasonable to expect him or her to sue before the statute ran on that conduct. This would be true in a case in which the conduct could be recognized as actionable harassment only in the light of events that occurred within the statute of limitations.

2. Additional Time for Verification of a Charge

The United States Supreme Court, in Edelman v. Lynchburg College, ___ U.S. ___, 122 S. Ct. 1145 (2002) recently resolved the controversy over the validity of an EEOC regulation interpreting Section 706(b) of the Civil Rights Act of 1964 that permits an otherwise timely but unverified charge to be verified after the time for filing a charge of discrimination has expired. The Supreme Court found that that this regulation was a permissible interpretation of Section 706(b) because:

[W]hile the verification process is meant to provide some degree of insurance against catchpenny claims of disgruntled, but not necessarily aggrieved, employees . . . Congress presumably did not mean to affect the nature of Title VII as a remedial scheme in which laypersons, rather than lawyers, are expected to initiate the process.

122 S. Ct. at 1150 (citations omitted).

B. Election of Remedies Under the Kentucky Civil Rights Act

Many state civil rights statutes, including the KCRA, provide both administrative and judicial avenues for relief. In Kentucky an individual may elect to pursue claims for discrimination under state law by filing a charge with the Kentucky Commission on Human Rights ("KCHR"), or with a local human rights commission, prior to filing a lawsuit under the KCRA. However, unlike claims brought pursuant to Title VII, the ADA and the ADEA, an individual bringing claims under the

KCRA may elect to forego the administrative process entirely, and immediately file a civil action in state or federal court. In recent years, there has been considerable debate in Kentucky over whether an individual's decision to initially proceed through the administrative process constitutes a binding election of remedies that would either prevent any future action in state or federal court under the KCRA or would at a minimum require exhaustion of the administrative process prior to the filing of a lawsuit.

The controversy over the effect of an initial election to pursue administrative relief is based on KRS 344.270 of the KCRA, which provides as follows:

A state court shall not take jurisdiction over any claim of an unlawful practice under this chapter while a claim of the same person seeking relief for the same grievance is pending before the commission. A final determination by a state court or a final order of the commission of a claim alleging an unlawful practice under KRS 344.450 shall exclude any other administrative action or proceeding brought in accordance with KRS Chapter 13B by the same person based on the same grievance.

The Kentucky Court of Appeals, in Founder v. Cabinet for Human Resources, 23 S.W.3d 221 (Ky. Ct. App. 1999), held that under this provision, if the complainant *chooses* to make an administrative filing, he has elected his remedy and may not thereafter proceed with a lawsuit under the KCRA in state or federal court. The Founder decision is based on the holding in Vaezkoroni v. Domino's Pizza, 914 S.W.2d 341 (Ky. 1995), an earlier Kentucky Supreme Court decision construing KRS 344.270. These two decisions interpreted this section of the KCRA as providing that the filing of a complaint with the state or local commission is subject matter jurisdictional, *i.e.*, once such a complaint has been filed, the circuit courts lose subject matter jurisdiction over the matter.

The Kentucky Supreme Court has not yet ruled on this issue; however, recent rulings by the Federal District Court in the Western District of Kentucky and a subsequent unpublished opinion issued by the Kentucky Court of Appeals appear to hold that where an individual has initially elected to use the administrative process, KRS 344.270 will only bar a subsequent action in state or federal court in two situations:

- (1) where the administrative agency has made a final determination that the charge has no merit, and has refused to provide the charging party with a Notice of Right to Sue following this determination; or
- (2) where the administrative proceeding is still pending before the administrative agency at the time the charging party files the lawsuit in state or federal court.

In Grego v. Meijer, Inc., 187 F. Supp. 2d 689 (W.D. Ky. 2001), the plaintiff filed a sex discrimination complaint with the KCHR in May 1998. She subsequently requested to withdraw her complaint. After the KCHR withdrew the complaint without prejudice, she filed a civil complaint in

the Jefferson Circuit Court, which the defendant employer then removed to federal district court on the basis of diversity jurisdiction. The Grego court denied the employer's subsequent motion to dismiss based on the doctrine of election of remedies. After examining the Vaezkoroni and Founder cases, the court declined to adopt their reasoning, based on its prediction that the Kentucky Supreme Court would not follow their holdings. Grego, 187 F. Supp. 2d at 693; *see also* Thomas v. Forest City Enterprises, Inc., 2001 WL 1772018 (W.D. Ky. Oct. 17, 2001).

Shortly thereafter, in Wilson v. Lowe's Home Center, 2001 WL 1658212 (Ky. Ct. App. Dec. 28, 2001), the Kentucky Court of Appeals rejected as dicta those portions of Vaezkoroni and Founder that would have prevented a charging party from filing suit in state or federal court after filing an administrative charge:

As we have noted, in the Vaezkoroni case the Kentucky Supreme Court stated that "[o]nce any avenue of relief is chosen, the complainant must follow that avenue through to its final conclusion."

Since the Vaezkoroni case involved an employee who had prosecuted his claims to the administrative body to a final determination, that language is clearly dicta.

Similarly, in the Founder case a panel of this court stated that "[f]rom our reading of the language in KRS 344.270 and Vaezkoroni once a complaint is filed with the Commission, a subsequent action in circuit court based on the same civil rights violation[s] is barred." Since the employee's circuit court complaint in Founder was barred by KRS 344.270 for lack of jurisdiction because the complaint was still pending with an administrative body, this language in the Founder case is also dicta.

Wilson, 2001 WL 1658212 at *7 (citations omitted).

Accordingly, it does not appear that the charging party, once having elected to proceed through the administrative process, is required to exhaust the administrative process prior to bringing a lawsuit under the KCRA. The charging party has the option of requesting to withdraw the charge of discrimination at any time during the administrative proceedings prior to a final determination on the merits by the administrative agency and then filing an action in state or federal court.

C. Admissibility of Evidence of Prior Sexual Conduct

1. Admissibility of Evidence of Prior Sexual Conduct of the Plaintiff

Federal Rule of Evidence (FRE) 412 as amended in December 1994, prohibits the admission of evidence offered to prove "other" sexual behavior (*i.e.*, behavior not intrinsic to the alleged misconduct) or the sexual predisposition of any alleged victim of sexual misconduct (including plaintiffs in sexual harassment cases) unless (a) the evidence is otherwise admissible under the federal rules and (b) its probative value substantially outweighs the danger of harm to any victim and

of unfair prejudice to any party. The Rule further prohibits evidence of an alleged victim's reputation unless it has been placed in controversy by the alleged victim.

The Advisory Committee Notes make clear that the procedures set forth in FRE 412 do not apply to *discovery* of a victim's past sexual conduct or predisposition in civil cases, which will continue to be governed by Federal Rule of Civil Procedure 26. Advisory Committee Notes at Subsection (c). However, the Advisory Committee Notes go on to provide:

In order not to undermine the rationale of Rule 412, however, courts should enter appropriate orders pursuant to Fed. R. Civ. P. 26(c) to protect the victim against unwarranted inquiries and to ensure confidentiality. Courts should presumptively issue protective orders barring discovery unless the party seeking discovery makes a showing that the evidence sought to be discovered would be relevant under the facts and theories of the particular case, and cannot be obtained except through discovery. In an action for sexual harassment, for instance, while some evidence of the alleged victim's sexual behavior and/or predisposition in the workplace may perhaps be relevant, non-workplace conduct will usually be irrelevant. *Cf. Burns v. McGregor Electronic Industries, Inc.*, 989 F.2d 959, 962-63 (8th Cir. 1993) (posing for a nude magazine outside work hours is irrelevant to issue of unwelcomeness of sexual advances at work). Confidentiality orders should be presumptively granted as well.

Recent cases construing amended FRE 412 in the context of admissibility at trial make it clear that the courts will apply it strictly according to its terms, and will also follow the Advisory Committee's guidance concerning the distinction between the admissibility of evidence concerning sexual conduct within the workplace and behavior outside work. For instance, in *Dufresne v. J.D. Fields & Co.*, 2001 WL 30671, 85 Fair Empl. Proc. Cas (BNA) 25 (E.D. La. Jan. 12, 2001), the court found evidence that a female employee downloaded Internet sex scenes from her office computer and e-mailed a copy to her manager on at least one occasion was relevant and probative both as to issue of whether the presence of pornography in the workplace was offensive to her and also to the appropriate measure of damages she could recover on her claim.

This case can be compared with *Wolak v. Spucci*, 217 F.3d 157 (2nd Cir. 2000), in which the plaintiff's hostile environment claim also relied on evidence that male co-workers placed pornographic magazines in areas where she would discover them. The *Wolak* court refused to allow the defendants to introduce evidence that the plaintiff had viewed pornographic movies outside work, finding that "whether an alleged victim in fact perceived her work environment to be sexually offensive does not turn on the private sexual behavior of the alleged victim, because a woman's expectations about her work environment cannot be said to change depending upon her sexual sophistication." *Id.* at 160. The evidence was not even considered to be probative as to the degree of distress the plaintiff might have suffered as a result of the pornography placed in the workplace, because:

Even if a woman's out-of-work sexual experiences were such that she could perhaps be expected to suffer less harm from viewing run-of-the-mill pornographic images displayed in the office, pornography might still alter her status in the workplace, causing injury, regardless of the trauma inflicted by the pornographic images alone.

Id. at 160-161.

However, the courts have shown a willingness to allow admission of evidence of conduct that occurred outside the workplace if the plaintiff discussed the conduct in the workplace. This was the case in Fedio v. Circuit City Stores, Inc., 1998 WL 966000 (E.D. Pa. Nov. 4, 1998), where the court held that because the plaintiff had discussed her sexual proclivities in the workplace, allowing her to invoke FRE 412 to prevent the admission of matters she had previously flaunted in public would be tantamount to a complete disregard of the rule's purpose.

In Chamblee v. Harris & Harris, Inc., 154 F. Supp. 2d 670 (S.D.N.Y. 2001), the plaintiff brought sexual harassment claims against her supervisor and employer, a McDonald's franchisee. The defendants sought to introduce evidence that the plaintiff had worked as a call girl prior to her employment with McDonald's, that she frequently made sexual statements at work, and that she told other employees that she was planning to open her own escort service in the future. Relying on Wolak v. Spucci, 217 F.3d 157 (2nd Cir. 2000) and the Advisory Committee Notes to the 1994 amendments to FRE 412, the court granted the plaintiff's motion to exclude evidence that she had previously worked as a call girl/escort prior to her employment with McDonald's. The court found that this evidence would only be relevant to prove her sexual disposition, a use plainly forbidden by Rule 412. However the court stated that the plaintiff's discussions with co-workers about her plans to start an escort service and her other sexual comments made at work were on a "different footing" than conduct that occurred outside work and might be admissible to refute her hostile work environment claims. *Id.* at 680.

Similarly, in Woodard v. Metro, I.P.C.T., 2000 WL 684101 (S.D. Ind. Mar. 16, 2000), the court held that evidence of the plaintiff's own sexual conduct in the workplace, including her workplace discussions of off-duty conduct, was relevant to show that she did not subjectively consider her work environment hostile and was also relevant for the purpose of evaluating whether her employer had responded reasonably to her complaint or whether the employer should have discovered the alleged harassment and responded earlier. The court found the probative value of the evidence that the plaintiff worked at a lingerie shop that she advertised and marketed while at Metro, that she wore provocative clothing, passed around photographs at work in which she was modeling lingerie and participated in sexual banter and horseplay while working at Metro, substantially outweighed its potential to unfairly prejudice her claims. *Id.* at *7.

2. Admissibility of Prior Acts of Alleged Harasser

Plaintiffs in harassment cases often attempt to bolster their claims by introducing evidence that the alleged harasser has engaged in acts of harassment or discrimination against others. Such attempts raise potential challenges under FRE 403 (relevance) and 404(b) (providing that evidence of

other crimes, wrongs or acts is not admissible to prove the character of a person in order to show action in conformity therewith, but may be admissible to prove motive, identity or absence of mistake or accident). Sometimes, such evidence is admitted for the purpose of showing that the employer had actual or constructive notice of the harasser's propensity for wrongdoing.

In Bank One, Kentucky, N.A. v. Murphy, 52 S.W.3d 540 (Ky. 2001), which is also discussed in Section [1.44], *supra*, the Kentucky Supreme Court reversed the summary judgment granted in favor of the employer on plaintiff's sexual harassment claim on the grounds that the plaintiff should have been permitted to present evidence concerning other prior acts of harassment by her alleged harasser. The court found that the employer's attempt to rely on the affirmative defense provided by Faragher v. City of Boca Raton, 524 U.S. 775 (1998), and Burlington Industries v. Ellerth, 524 U.S. 742 (1998), made evidence concerning prior harassment of a different employee by the same alleged harasser relevant. Evidence of the prior harassment, and the insufficiency of the employer's response to the harassment complaint that was made as a result of the prior harassment, could be used to refute the employer's assertion that it took reasonable efforts to prevent harassment in the workplace.



**INSURANCE COVERAGE FOR EMPLOYMENT
DISCRIMINATION AND HARASSMENT CLAIMS**

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SECTION F



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DISCRIMINATION AND HARASSMENT CLAIMS**

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**INSURANCE COVERAGE FOR EMPLOYMENT
DISCRIMINATION AND HARASSMENT CLAIMS**

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I BACKGROUND.

- A. 17% of cases brought in federal court allege civil rights violations. The number of wrongful employment practices charges received by EEOC increased from 59,000 in 1989 to nearly 90,000 in 1995. The number of employment discrimination cases increased by 47% from 1989 to 1995.
- B. Costly to employers.
 - 1. Legal fees.
 - 2. Disruption in business.
 - 3. Adverse media attention.
 - 4. Judgment.
- C. Liability of attorney for failing to advise of possible insurance coverage. *Jordache Enterprises, Inc. v. Brobeck, Phleger & Harrison*, 56 Cal.Rptr.2d 661 (1996) (rev'd); *Darby & Darby, P.C. v. VSI International, Inc.*, 678 N.Y.S.2d 482 (1998) (rev'd).

II INSURANCE LINGO

- A. ISO.
- B. Hammer clause.
- C. Claims made policy.
- D. Reservation of rights. *Eskridge v. Educator and Executive Insurers, Inc., Ky.*, 677 S.W.2d 887 (1984).

III RULES FOR INTERPRETING INSURANCE POLICIES.

- A. Terms of insurance contracts have no technical meaning in law and are to be interpreted according to the usage of the average man and as they would be read and understood by him in the light of the prevailing rule that uncertainties and ambiguities must be resolved in favor of the insured. *Fryman v. Pilot Life Insurance Company*, Ky., 704 S.W.2d 205 (1986).
- B. An ambiguous policy is to be construed to effectuate the purpose of indemnity. *James Graham Brown Foundation, Inc. v. St. Paul Fire & Marine Insurance Co.*, Ky., 814 S.W.2d 273 (1991); *Wolford v. Wolford*, Ky., 662 S.W.2d 835 (1984).
- C. Insurer has duty to defend if there is any allegation which potentially, possibly or might come within the coverage of the policy, and the insurance company must defend any suit in which the language of the complaint would bring it within the policy coverage regardless of the merits of the action. *O'Bannon v. Aetna Casualty and Surety Company*, Ky., 678 S.W.2d 390 (1984); *Wolford, supra*.
- D. The determination of whether a defense is required must be made at the outset of the litigation. *Knapp v. Chevron USA, Inc.*, 781 F.2d 1123 (5th Cir. 1986); *but see Transamerica Insurance Company v. KMS Patriots, L.P.*, 752 N.E.2d 777 (Mass. App. 2001).
- E. Duty to defend continues to the point of establishing that liability upon which plaintiff was relying was in fact not covered by the policy and not merely that it might not be. 7C Appleman, *Insurance Law and Practice* § 4683.01 (Berdal Ed. 1979).
- F. The duty to defend is broader than the duty to indemnify. *Wolford, supra*. If some claims are covered and others are not, the insurer has a duty imposed by law to defend the action in its entirety because to defend meaningfully, the insurer must defend immediately, and to defend immediately it must defend entirely.

IV TYPES OF EMPLOYMENT RELATED CLAIMS.

- A. Wrongful termination.
- B. Defamation.
- C. ERISA.
- D. FMLA.

- E. Discrimination based on protected class.
- F. Disability claims.
- G. Fraud.
- H. Contract.
- I. Harassment.
- J. Intentional infliction of severe emotional distress. *Wilson v. Lowe's Home Center*, Ky. App., 2001 WL 1658212 (2001).
- K. Violations of Employee Polygraph Protection Act.
- L. Whistle blower claims.
- M. Retaliation, workers' compensation.
- N. Public policy.
- O. Invasion of privacy.
- P. Negligent supervision, hiring, etc.
- Q. Dangerous workplace.
- R. Due process.
- S. Wage and hour.

V POSSIBILITIES OF INSURANCE COVERAGE.

- A. Workers' Compensation.
 - 1. Excludes intentional acts.
 - 2. Certificates for self-insureds.
 - 3. Employment liability section (sometimes called "B" coverage).
 - 4. Endorsements.

- B. Comprehensive General Liability (“CGL”).
1. Coverage A for bodily injury (does not include emotional damages), coverage B for advertising injury, and coverage C for medical expenses. Some also cover “personal injury” which is defined as injury other than bodily injury.
 - a. *Smith v. Animal Urgent Care, Inc.*, 542 S.E.2d 827 (W.Va. 2000). Former employee alleged sexual harassment, wrongful discharge, and intentional infliction of severe emotional distress. The policy provided coverage for bodily injury. The Court held that purely mental and emotional harm that arises from a claim of sexual harassment and lacks physical manifestation does not fall within the definition of bodily injury. (Policy also provided coverage for “personal injury” but the Court failed to address coverage for claim under that provision.)
 2. Must be a result of an “occurrence” (an accident).
 - a. *Smith, supra*. Court held that it strains the imagination to speculate how a pattern of sexual overtones and touching can be accidental. *See also Thompson v. West American Insurance Company*, Ky. App., 839 S.W.2d 579 (1992), where the Court commented: “We believe that sexual molestation is so inherently injurious, or substantially certain to result in some injury, that the intent to injure, or the expectation that injury will result, can be inferred as a matter of law.”
 3. Employment related practices exclusion (Insurance Services Offices 1993) typically excludes injuries to employees “arising in and out of the course of employment.”
 - a. *Agricultural Insurance Co. v. Focus Homes, Inc.*, 212 F.3d 407 (8th Cir. 2000). Insurers provided CGL coverage, PL (professional liability) coverage, and CU (commercial umbrella) coverage to employer. Three women asserted a cause of action for sexual harassment, based on an allegation that they were sexually assaulted by a retarded male in the employer’s treatment facility. The Court concluded that the conduct came within the definition of bodily injury, but held that the CGL coverage did not apply based on an employer’s liability exclusion, which excluded coverage for bodily injury of an employee arising out of and in the course of employment. *See also Smith, supra*.
 - b. *Golden Eagle Insurance Corp. v. Rocky Cola Café, Inc.*, 94 Cal. App.4th 120, 114 Cal.Rptr.2d 16 (2001). CGL insurer sought declaration that it had no duty to defend its insureds (employer and several employees) against an action brought by a former waitress who alleged sexual harassment, defamation, retaliation, intentional infliction of severe emotional distress, wrongful termination and negligent hiring and supervision. The defamation claim was based on the assertion that a superior of the waitress communicated to others

that she was "sexually promiscuous and a calculating bitch who had, by use of sexually aggressive tactics, maneuvered him into an unwanted sexual relationship in order to obtain on-the-job favors." The complaint also alleged that his statements were republished by other named defendants. The insurer admitted that certain aspects of the defamation claim fell within the definition of "personal injury" contained in the policy, but asserted that coverage was not provided based on an exclusion for injuries arising out of any employment related practices, policies, acts or omissions. The Court held that the exclusion did not apply because it was difficult to conclude that the comments in issue were employment related.

4. Intentional Acts Exclusion.

- a. *Smith, supra*. Court held that acts of sexual misconduct constitute intentional acts. It further held that employer's attempt to obtain coverage by contending that some of the claims were based on negligence (negligent supervision of the harasser) was a transparent attempt to trigger insurance coverage. (Note that some courts have reached the opposite conclusion.)

C. Directors and Officers Liability ("D & O").

1. Usually no coverage for company or others.
2. Employment practices liability coverage endorsement ("EPL") broadens coverage for all employees and deletes exclusions for bodily injury and emotional distress.
3. Usually contains exclusion for claims based on bodily injury, or any claim for emotional distress or mental anguish.
 - a. *Philadelphia Indemnity Insurance Co. v. Maryland Yacht Club, Inc.*, 742 A.2d 79 (Md. App. 1999). Former employee alleged that his discharge was an act of retaliation for filing a workers' compensation claim. Insurer had issued a D & O policy, which contained an exclusion for bodily injury. The Court held that the former employee's claim was not within the scope of the exclusion, even though the Court recognized that Maryland does not follow the majority rule that an insurance policy is to be construed strongly against the insurer.

D. Errors and Omissions, Professional Liability, and Malpractice Coverages.

1. Normally economic and emotional distress covered.
 - a. *Agricultural Insurance Co., supra*. PL policy covered those sums which the insured becomes obligated to pay because of professional error or mistake made arising out of the performance or failure to perform any professional service for others. The Court held that the policy did not provide coverage for two reasons. First, the complaint did not allege injuries arising out of professional malpractice.

Second, coverage was barred by an exclusion of injuries occurring in the course of employment.

- E. Employment Practices Liability Insurance ("EPLI").
1. Sold by approximately 75 carriers as stand alone policies or endorsements to D & O coverage.
 2. Standardized policy available in 1998, but few insurers adopted.
 3. Claims made coverage.
 4. Covers company, officers, directors and employees (be careful regarding definitions of employee that do not include leased or seasonal employees).
 5. Covers "claims," which may include arbitration and administrative proceedings.
 6. Issue if just covers claims by employees, or includes claims brought on employee's behalf; also be wary that the definition of employee may not cover applicants for job (claim based on failure to hire).
 7. Focus on what acts covered (wrongful dismissal; discharge; termination; wrongful failure or refusal to hire or promote; wrongful discipline or demotion; failure to grant tenure; negligent evaluation; sexual harassment; other types of harassment; hostile work environment; employment discrimination; invasion of privacy; defamation; wrongful infliction of severe emotional distress; failure to provide for or enforce adequate or consistent employment policies or procedures; retaliation; and violations of FMLA.
 8. Typical exclusions:
 - a. Cost of reasonable accommodations.
 - b. Claims based on Fair Labor Standards Act.
 - c. Claims based on National Labor Relations Act.
 - d. Claims based on violations of the Worker Adjustment and Retraining Act.
 - e. Claims based on violations of COBRA.
 - f. Claims based on violations of OSHA.
 - g. Claims based on violations of ERISA.
 - h. Costs associated with non-monetary and injunctive relief.
 - i. Claims arising from downsizing, layoffs, plant closures and strikes.
 - j. Punitive damages.
 9. Other considerations.
 - a. Notice obligations.
 - b. Duty to defend.
 - c. Choice of counsel.
 - d. Settlement authority and hammer clause.
 10. Note that in the *Smith* opinion the Court commented in its decision finding against the insured on CGL policy that EPLI policies were created specifically for employment related actions.

F. Commercial Umbrella Coverage

1. Employment practices exclusion (“arising out of refusal to employ, termination of employment, coercion, demotion, evaluation, reassignment, discipline, humiliation, discrimination, or other employment related practices, policies, acts or omissions”).
 - a. *SCI Liquidating Corp. v. Hartford Insurance Co.*, 526 S.E.2d 555 (Ga. 2000). Three former employees obtained a judgement against SCI for sexual harassment. SCI filed suit against Hartford Fire, its CGL insurer, and Hartford Casualty, its umbrella carrier, seeking to recover the amount of the judgment. The Eleventh Circuit determined that the umbrella policy’s bodily injury provision did not provide coverage to SCI for the sexual harassment, but that the employees’ allegations of discrimination appeared to be covered by the umbrella’s definition of personal injury. The Court noted that the policy had an exclusion for claims made by employees for personal injury arising out of and in the course of employment. It certified to the Supreme Court of Georgia the issue of whether the conduct in issue could be construed to have arisen in and out of the course of employment. The Georgia Supreme Court ruled that the injuries did not arise in and out of the course of the employment and, therefore, the exclusion did not apply. The opinion noted that the Eleventh Circuit had determined that the CGL policy did not provide coverage, but did not give an explanation.
 - b. *Agricultural Insurance Co.*, *supra*. Court held that conduct fell within definition of bodily injury, but that the employment practices provision excluded coverage.

VI OTHER COVERAGE ISSUES.

A. Public Policy Violations.

1. *Doe v. Shaffer*, 738 N.E.2d 1243 (Ohio 2000). Ohio Supreme Court held that it would violate public policy for a liability insurance carrier to provide coverage to diocese and bishop for their negligence related to sexual abuse committed by others. This appears to be a minority view.

VII CONSIDERATIONS FOR COVERAGE AND PREMIUMS.

- A. Workplace composition.
- B. Counsel advice.
- C. Claim experience.

- D. Handbook (including counsel's endorsement).
- E. Training.
- F. Evaluations.
- G. Written grievance procedure.
- H. Human resource manual.
- I. Established termination procedure.
- J. Employee assistance program.
- K. Policy for handling complaints of harassment.

VIII ETHICAL CONCERNS WHEN REPRESENTING EMPLOYER OR EMPLOYEE THROUGH INSURANCE CARRIER: E-416; E-410; E-409; E-404; E-378; E-368; E-359; E-340; E-331.

- A. Control of defense by insurer.
- B. Settlement.
- C. Certain claims covered, others not.
- D. Audits.
- E. Billing procedures.
- F. Representation of numerous defendants, and control by employer or insurer.

KBA E-416

Question 1: In general, may an insurance defense lawyer agree to abide by insurer-prescribed case handling guidelines in representing the insured?

Answer: A lawyer may *not* agree to abide by such guidelines *unless*:

- a) the lawyer determines that the guidelines will not interfere with the lawyer's independent professional judgment and other duties owed to the insured under the Kentucky Rules of Professional Conduct; and
- b) the lawyer discloses the guidelines' existence to the insured, and provides a practical explanation of their import, at the outset of the representation and as may become necessary in specific situations thereafter, and the insured consents after consultation to any guideline that materially limits the representation; and
- c) the lawyer, upon undertaking the representation, performs all duties imposed by the Rules, regardless of compensation under the guidelines, so long as the representation continues.

Every lawyer is *strongly cautioned* that the insured is entitled to adequate representation despite limitations prescribed by the insurer. A lawyer who is unable or unwilling to accept the potential burden of this responsibility must decline the representation at the outset.

Question 2: More particularly, may the lawyer accept representation under guidelines that:

- a. Require approval by the insurer before the lawyer undertakes any discovery, conducts any legal research, or files any motion?

Answer: *No.* The lawyer may agree, however, to guidelines setting a reasonable, tentative budget and providing a process for ongoing consultation.

- b. Require all investigative work or all records review to be performed only by the insurer's employees or, if performed by the lawyer's firm, to be billed only at a paralegal rate?

Answer: *No.* The lawyer may agree, however, to guidelines establishing an appropriate allocation of lawyer and nonlawyer/paralegal tasks, or setting a reasonable tentative budget for investigative work or document review, and providing a process for ongoing consultation.

- c. Require prior approval of compensation for additional lawyers or experts with whom the principal lawyer may wish to confer, or for a lawyer's trial preparation exceeding a specified pretrial period (e.g., thirty days)?

Answer: *Yes,* if (and only if) such limitations are reasonable in relation to the issues in the case and the guidelines provide a process for ongoing consultation.

- d. Prescribe detailed billing and reporting procedures, with deadlines for certain submissions?

Answer: Yes, if (and only if) such procedures and deadlines do not create material disincentives to adequate representation of the insured and do not abridge the insured's right to confidentiality.

Even when a lawyer is permitted ethically to accept representation under an insurer's guidelines, he or she may choose not to do so. The lawyer is free to decline the representation, just as the insurer is free to offer the work to other counsel. The lawyer must decline, however, if he or she is unable or unwilling to provide adequate representation to the insured regardless of limitations prescribed by the insurer.

Principal References:

KBA Ethics Opinions E-331, 340, 359, 368, 378, 404, 409, 410.

ABA Formal Opinion 96-403

S.C.R. 3.130 [Kentucky Rules of Professional Conduct], Rules 1.1, 1.2, 1.3, 1.6, 1.7(b), 1.8(f), 1.16, 5.4.

American Insurance Association v. Kentucky Bar Association, 917 S.W.2d 568 (Ky. 1996).

In the Matter of the Rules of Professional Conduct and Insurer Imposed Billing Rules and Procedures, 2 P.3d 806 (Mont. 2000)

2 AMERICAN LAW INSTITUTE, RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS (2000) §§ 121, 122, 134.

1 G. HAZARD & W. HODES, THE LAW OF LAWYERING (3d ed. 2000) §§ 12.13, 12.14.

Additional references, including ethics opinions from other states, appear throughout the text.

Opinion:

Our analysis proceeds in four steps. First, we place the insurance guidelines issue in context by recalling previous opinions of this Committee and by noting the polarized contentions of partisans in the current nationwide debate over guidelines. Next, we examine professional responsibility in an insurance defense context, focusing on the key principles of informed consent by clients and independent professional judgment by lawyers. Then, we apply these principles to the general issue of insurer-prescribed case handling guidelines. Finally, we comment on particular limitations contained in some guidelines.

A. History and Current Controversy

A purchaser of a liability insurance policy acquires two things of value: an indemnity fund to pay claims covered by the policy, and an insurer-provided legal defense against the claims. *E.g.*, *Wolford v. Wolford*, 662 S.W.2d 835 (Ky. 1984). For insurers, the cost of providing the legal defense has become a major concern. Defense costs are significant components of total litigation expenses, which were reported recently to consume "nearly 55 cents of every claim dollar" in property-casualty insurance. Sullivan & Muldowney, "Changing Times in the Insurance Industry," *For the Defense* (Defense Research Institute, Feb. 1998), Supp. p. 2, *quoted in* Indiana State Bar Ass'n Legal Ethics Committee,

Op. 3 (1998). Cost containment, viewed by insurers as an urgent imperative, has generated ethical concerns that have found their way to our Committee.

In Opinion KBA E-331, issued in 1988, the Committee considered a broad inquiry as to whether any ethical problems could arise if a liability insurer "instruct[ed] defense counsel to conduct or limit a defense so as to minimize the insurer's costs," even though the claim was within coverage limits. The Committee answered "yes," but disavowed "any generalization" on the question. The tone was cautionary, not prescriptive:

We issue this opinion only to advise of ethical considerations that may arise in this context. We are not suggesting that counsel has carte blanche to needlessly run up a bill. Such conduct would be just as reprehensible as yielding professional control of his or her work to an adjuster or claims manager. Nor are we suggesting that costs and expenses are not a legitimate concern of the insurer. Conflicts are not inevitable, or irreconcilable. Presumably these matters can be resolved amicably and responsibly in the great majority of cases. We only wish to emphasize that the insured is defense counsel's client, and that counsel owes professional obligations to his or her client that flow from the attorney-client relationship and are not bounded by the "hardboiled commercial" relationship between the insured and the insurer.

Five years later, the Committee approved, with some caveats, an attorney fee arrangement creating an incentive (i.e., a "reverse" contingent fee) for insurance defense counsel to achieve the best outcome on the claim. See Opinion KBA E-359 (1993). Such an arrangement was not perceived to create a conflict between the lawyer and the insured client. The following year, however, when the Committee returned to the subject of litigation costs -- as opposed to indemnity payments -- it encountered a "hardboiled commercial" approach to cost containment. The question was whether a lawyer could contract with an insurance carrier to do all defense work for a set fee, or could agree to take such work while foregoing reimbursement of all litigation costs (experts, court reporters, etc.). Answering both questions "no," the Committee noted that such arrangements would interpose the lawyer's economic interests directly against those of the insured client. The Committee acknowledged that such an economic tension "is inherent in other lawyer-client arrangements; but here the insured client ... [would] have no control over the choices that will be made." See Opinion KBA E-368 (1994). As explained more fully below, the Committee's opinion was later endorsed by the Supreme Court of Kentucky in *American Insurance Association v. Kentucky Bar Association*, 917 S.W.2d 568 (Ky. 1996) (hereinafter *AIA*).

Today, upon inquiry from an organization of Kentucky defense lawyers, the Committee must examine the ethical dimensions of a more complex and nuanced form of cost containment: insurer-prescribed case handling guidelines. Such guidelines vary widely from insurer to insurer, and their actual administration may vary from case to case, but they have certain core characteristics. As suggested by the term "guidelines," they often contain disclaimers of any intent by the insurer to override a lawyer's ethical duties; nonetheless, the guidelines usually are expressed as conditions of a lawyer's engagement to represent the insured client. They mandate the form and timing of a law firm's billings and reports, and they warn that no payment will be made for unauthorized expenses or for services that are outside the guidelines and not otherwise approved. They usually limit (absent prior approval) the number and identity of lawyers working on a case at any particular stage, the extent of motion practice or discovery to be conducted, and the amount or manner of legal research to be undertaken, on the client's behalf.

These guidelines have generated national controversy in academic, professional, and judicial venues. In several respects, unfortunately, the controversy has come to resemble a minefield of false dichotomies. Guideline opponents contend that the controversy is about ethics; proponents argue that it is only about economics. Opponents decry a loss of the lawyer's independent professional judgment under the Rules of Professional Conduct; proponents declare that the insurer has a contractual right to control the defense of claims covered by the insurance policy. Opponents maintain that the lawyer has but one client, the insured; proponents assert the lawyer has obligations to the insurer regardless of whether the insurer is deemed a co-client or merely a third-party payer. Opponents complain that the guidelines reduce defense practice and the needs of each client to a formulaic regime, often administered on behalf of insurers by poorly trained and overworked nonlawyer case managers. Proponents respond that the guidelines allow for exceptions when justified and provide a framework for dialogue between counsel

and insurers. The Committee finds, for reasons appearing below, that that each of these contentions has some merit, and some limitation. Distilling the truth of both sides is essential to making sense of the guidelines controversy.

B. Professional Responsibility and Insurance Defense

Insurance has been described as “a regulated industry clothed with a substantial public interest.” 7C J. A. APPLEMAN, *INSURANCE LAW AND PRACTICE* 2 (W. F. Berdal ed. 1979). Subject to legislative and administrative oversight (which varies considerably in quality and intensity from state to state), liability insurance companies collect premiums, invest funds, and pay claims. To secure protection against unwarranted or excessive claims, insurers generally are authorized to contract with policyholders for control and settlement of litigation. *Id.* at 2-4. Most insurance policies contain such provisions; moreover, they treat an insurer-provided defense as an obligation. Thus, the insurer’s right of control is linked to fulfillment, in good faith, of the insurer’s duty to defend. R. E. KEETON & A. I. WIDISS, *INSURANCE LAW: A GUIDE TO FUNDAMENTAL PRINCIPLES, LEGAL DOCTRINES, AND COMMON PRACTICES* (1988) § 7.6(b). Conversely, the insured has a contractual duty to cooperate in the defense and, absent conflicting interests, is deemed to have consented to the role of the insurer in designating defense counsel. *Id.*

Juxtaposed against this regulatory and contractual authority of the insurer are the case law and Rules of Professional Conduct regulating the relationship between a lawyer and client. In Kentucky (as noted in Opinions E-331 and E-368 cited above), when an insurance company engages a lawyer to defend an insured against a claim, the insured – not the insurer – is the lawyer’s client. The one-client doctrine also has been articulated in this Committee’s Opinion KBA E-410 (1999) (stating, *inter alia*, that absent informed consent by the insured, defense counsel may not reveal to the insurer confidential information obtained from the insured that could adversely affect coverage); in Opinions KBA E-409 (1999) and E-404 (1998) (both stating that insurance defense counsel must obtain the insured client’s full and informed consent before submitting billing information to the insurer’s outside auditor); in Opinion KBA E-378 (1995) (counsel engaged to represent the insured may not also defend the insurer against an unfair settlement practices claim arising from same action); and in Opinion KBA E-340 (1990) (insurance defense counsel may not permit the insurer’s representative to sit in on the lawyer’s conferences with the insured without the insured’s informed consent).

Kentucky’s one-client view differs from the position taken in some states, and expressed by some commentators, that the tripartite relationship (or “eternal triangle”) of insured, insurer, and defense counsel actually entails two clients: the insured and the insurer. *See, e.g.*, Maryland State Bar Ass’n Comm. On Ethics, Op. 00-23 (2000); State Bar of Wisconsin Ethics Opinions, Op. E-99-1 (1999); E. Cothran, *Can Carriers Legitimately Evaluate Independent Counsel Fees without Impeding Counsel’s Independent Judgment?* Vol. 29, No. 3, *THE BRIEF* (ABA Tort & Insurance Practice Section, Spring 2000), at 38-46; K. Syverud, *The Ethics of Insurer Litigation Management Guidelines and Legal Audits*, *INS. LITIG. REP.* (May 1, 1999), at 180-94; D. Richmond, *The Business and Ethics of Liability Insurers’ Efforts to Manage Legal Care*, 28 *U. MEM. L. REV.* 57 (1997). Kentucky’s view, however, is shared by many other states. *See, e.g.*, In the Matter of the Rules of Professional Conduct and Insurer Imposed Billing Rules and Procedures, 2 P.3d 806 (Montana 2000) (hereinafter *Montana Rules*); Rhode Island Supreme Court Ethics Advisory Panel Opinion No. 99-18 (1999); Alabama Ethics Opinions, Op. RO-98-02 (1998). *See generally* J. Pitulla, *Three-Way Street: Discord between Insurers and Insureds Puts Defense Lawyers on Perilous Path*, 81 *A.B.A.J.* 102 (August, 1995) (characterizing single-client view as the majority approach); D. O’Roark, *In Kentucky the Insured is Your Client – Not the Insurer!* *KY. BENCH & BAR*, vol. 60, no. 1 (Winter 1996), 49-52 (observing that Kentucky’s one-client view is “with the national trend”). The one-client view also has received favorable scholarly commentary. *E.g.*, 1 G. HAZARD & W. HODES, *THE LAW OF LAWYERING* (3d ed. 2000) (hereinafter *Hazard & Hodes*), at §12.14; S. Pepper, *Applying the Fundamentals of Lawyers’ Ethics to Insurance Defense Practice*, 4 *CONN. INS. L. J.* 27 (1997).

Under the one-client view, the insurer is a third-party payer, not a client. Third-party payment is a

phenomenon seen not only in insurance defense cases, but also in litigation involving persons represented by lawyers in public legal aid programs or private pre-paid legal service plans; cases involving officers of corporations, or members of organizations, who are represented by entity-hired attorneys; and litigation in which lawyers have been engaged by the parties' friends or families. See generally, *Hazard & Hodes* §12.13. Among third-party arrangements, however, the insured-insurer-defense counsel relationship may be unique because it is rooted in an underlying contract and involves "primarily standardized protection afforded by a regulated entity in recurring situations." 2 AMERICAN LAW INSTITUTE, RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS (2000) (hereinafter *Third Restatement*), at §134, comment *f*. As noted above, the insurer has contracted to provide a defense and it possesses a correlative right to control the defense. This right of control, however, is limited by another source of law: the cases and ethical rules governing lawyer-client relations.

In case law, it appears well settled as a general proposition that a lawyer may accept direction from a person other than the client if, but only if, (a) the direction does not interfere with the lawyer's independence of professional judgment; (b) the direction is reasonable in scope and character, e.g., reflecting obligations borne by the person directing the lawyer; and (c) the client gives informed consent to the direction. See, *Third Restatement* § 134 (2) (cross-referencing §§ 121, 122). This three-part test applies regardless of whether the person giving the direction is a third-party payer or another client. See comment *f* to *Third Restatement* § 134; see generally, ABA Formal Opinion 96-403 (1996) (hereinafter *ABA Opinion*) (upholding insurer's right to give direction regarding settlement within policy limits, while noting that insured who objects can assume responsibility for his or her own defense, and declaring that "[f]or the purposes of this opinion, nothing fundamental turns on whether the lawyer represents the insured alone or both the insurer and the insured"). Generally speaking, when the three-part test is fully satisfied, the client is deemed to have conferred the power of directing the defense to the insurer. *Third Restatement* § 134, comment *d*.

If this three-part test were applied to an insurance company directive to defense counsel on the conduct of litigation, element (b) -- the requirement of reasonableness -- might be satisfied simply by the insurer's obligation to pay for the defense. But element (c), the requirement of informed consent by the insured, would require more than the bare language of the insurance contract; and element (a), the requirement of noninterference with the lawyer's independent professional judgment, would be even more problematic. As this Committee noted in Opinion E-331, and as our Supreme Court later recognized in *ALA*, the interests of insurers and insureds are subject to wide divergence, even in cases where claims appear to fall within the subject-matter coverage and dollar limits of the insurance policy. An insured may have a reputational stake in the case, or may have another legitimate personal interest, that could be affected adversely by the insurer's direction to counsel concerning discovery, settlement, trial or appeal. In such a situation, counsel's candid advice to the client might be contrary to the insurer's strategy. Moreover, the perceived interests of the insured and insurer can evolve -- just as coverage issues and claim values can evolve -- while litigation progresses. Accordingly, in the insurance defense context, an insured's acts of conferring the power of direction upon the insurer (signing the insurance contract and giving informed consent at the outset of the representation) are subject to change if substantial risks to the insured's interests become apparent during the representation. *Third Restatement* § 134, comment *f*.

The requirements of informed consent and independent professional judgment, and the necessity of satisfying those requirements throughout the litigation, also emerge when the question of insurance company directives is examined in light of the Kentucky Rules of Professional Conduct (S.C.R. 3.130). Under Rule 1.2 (c) and comment 4 to the rule, an insurer's directive requires the insured's informed consent -- i.e., a consent "after consultation" (not merely a consent implied by the insurance contract) -- if the directive limits the objectives of the representation. Similarly, counsel's right to accept direction from a person other than the client is recognized, but limited, by Rule 1.7 (b), which provides in pertinent part as follows:

A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:

- (1) The lawyer reasonably believes the representation will not be adversely affected; and
- (2) The client consents after consultation

Thus, Rule 1.7 (b) echoes the necessity of consultation with the insured and also requires that counsel determine independently that the representation – shaped by the objectives established under Rule 1.2 (c) – will not be adversely affected. As mentioned in Comment 4 to Rule 1.7, the reasonableness of the lawyer's belief that the representation will not be adversely affected must be measured by the standard of a disinterested lawyer. Moreover, the adequacy of consultation must be considered in light of Rule 1.4, which requires a lawyer to keep the client "reasonably informed" and to "explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation." See also Opinion KBA 410 (1999). The disclosure should occur at the outset of the representation and periodically thereafter when specific circumstances so require. It must be "sufficient to permit the client to appreciate the significance of the matter in question," and it may take the form of a "short letter clearly stating that the lawyer intends to proceed at the direction of the insurer in accordance with the terms of the insurance contract and what this means to the insured." *ABA Opinion at 2*. See generally, *Third Restatement* § 134, comment f.

Rule 1.8(f) repeats the reference to consultation and makes explicit the protection of independent professional judgment in a third-party payment situation:

A lawyer shall not accept compensation for representing a client from one other than the client unless:

- (1) Such compensation is in accordance with an agreement between the client and the third party or the client consents after consultation;
- (2) There is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship; and
- (3) Information relating to representation of a client is protected as required by Rule 1.6.

Although the wording of Rule 1.8 (f) differs somewhat from that of Rule 1.7 (b) above, the two rules are intended to provide the same protection for counsel's independence of professional judgment. *Hazard & Hodes* § 12.13. Rule 5.4(c) further reinforces that protection, as follows:

A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services.

Indeed, the thrust of Rule 5.4 in its entirety is to safeguard the professional independence of a lawyer. The importance of professional independence is underscored by Rule 5.4 (d) (2), which prohibits a lawyer from practicing with a for-profit entity in which a nonlawyer has the right to direct or control the lawyer's professional judgment. Although Rule 5.4 (d) (2) does not apply by its literal terms to insurance defense retainers, it highlights the general need under Rule 5.4 (c) and the other rules cited above to scrutinize arrangements in which a lawyer regularly receives direction from a nonlawyer, such as an insurance company's claims manager.

The rules -- with their thematic emphasis upon ongoing informed consent by clients and upon the exercise of independent professional judgment by lawyers -- are part of a comprehensive ethical framework that shapes all lawyer-client relationships. Within this framework, the requirements of informed consent and independent professional judgment secure the insured client's entitlement to competent legal services (Rule 1.1) and the right to understand any material limitations upon the scope and objectives of the insurer-supplied representation (Rule 1.2). The lawyer is expected to act with

reasonable diligence and promptness (Rule 1.3), keeping the insured informed (Rule 1.4), protecting the insured's confidences (Rule 1.6), and rendering candid advice (Rule 2.1 and comments to Rule 1.7). Counsel must perform these duties without charging the insurer more than a reasonable fee (Rule 1.5). These duties comprise a professional mandate that continues until the relationship concludes or is terminated in a manner permitted by Rule 1.16. A lawyer may not narrow his or her duties, by accepting direction that limits the objectives of the representation, unless the client consents after consultation and the lawyer concurs, exercising independent professional judgment. In any event, the representation may not be so limited as to impair the competence of legal services as required by Rule 1.1. (See Comment 5 to Rule 1.2.)

C. Informed Consent, Independent Professional Judgment, and Case Handling Guidelines

The principles of informed consent and independent professional judgment are foundations of insurance defense, although their importance has not always been recognized. During much of the twentieth century, the insurer's contractual right to control the litigation, subject to an implied covenant of good faith, was considered the dominant force in the insurer/insured/defense lawyer relationship. *E.g.*, *Gribaldo, Jacobs, Jones & Associates v. Agrippina Versicherungen A. G.*, 476 P.2d 406 (Cal. 1970) (upholding policy provision that forbade incurring defense costs without the insurer's prior consent, and holding that the provision could be ignored only if the insured had requested and had been denied a defense by the insurer). More recent decisions, however -- such as the Kentucky Supreme Court's opinion in *ALA* -- have made it clear that insurance defense lawyers must follow the case law and rules of professional responsibility that define and safeguard the lawyer-client relationship. This does not mean, however, that insurers' contractual rights have disappeared or that lawyers today may simply disregard all efforts by insurance companies to control litigation costs. Rather, the issue has become whether, and to what extent, such cost controls intrude upon informed consent and independent professional judgment.

The potential variety of insurer-prescribed case handling guidelines makes it impossible to eschew or embrace all of them categorically. Our Committee recognized in Opinion E-331 that guidelines must be evaluated on a case-by-case basis. Referring to fees and expenses incurred by defense counsel, the Committee said:

[T]he insurer has a legitimate interest in keeping such costs down. ... *At some point* [however], carrier imposed restrictions may threaten counsel's ability to provide [zealous and competent] representation and impact on the lawyer's ability to bring to bear his independent professional judgment on behalf of the insured. [Emphasis supplied.]

Later, when our Supreme Court in *ALA* upheld this committee's Opinion E-368, the Court similarly stopped short of declaring all insurer-imposed guidelines invalid. In fact, the Court declared that "the ethics opinions and case law cited in E-368 are on point...." 917 S.W.2d at 573. As noted above, Opinion E-368 cited Opinion E-331, in which this Committee sounded a warning about insurer-imposed budget limitations but was careful not to lay down a categorical prohibition.

Our long-standing view, that insurer-prescribed guidelines must be examined in each case to determine their impact upon informed consent and independent professional judgment, is also expressed in the ethics opinions of many other states. Indeed, the case-by-case approach appears to be nearly universal, so far as our research discloses. *See, e.g.*, Alabama State Bar Disciplinary Commission Opinion No. RO-98-02 (1998); Colorado Bar Association Ethics Committee Formal Opinion No. 107 (1999); Florida Bar Association Ethics Committee Opinion No. 97-1 and Staff Opinion 20591 (1997); Hawaii Supreme Court Disciplinary Board Opinion 37 (1999); Idaho State Bar Committee on Ethics Opinion No. 136 (1999); Indiana State Bar Association Legal Ethics Committee Opinion No. 3 (1998); Iowa Supreme Court Board of Professional Ethics and Conduct, Opinion No. 99-01 (1999); Mississippi Bar Ethics Committee Opinion No. 246 (1999); New York State Bar Association Committee on Professional Ethics Opinion 721 (1999); Rhode Island Supreme Court Ethics Advisory Panel Opinion No. 99-18 (1999); Tennessee Supreme Court Board of Professional Responsibility Formal Ethics Opinion 2000-F-145 (2000); Wisconsin State Ethics Opinion E-99-1 (1999). These opinions, as we read them, do not

categorically preclude *all* insurer-prescribed guidelines, but allow defense counsel to accept them to the extent they do not significantly encroach upon the principles governing the attorney-client relationship. *Accord, Third Restatement*, at § 134, comment *f*, particularly Illustration 5, at p. 409.

Some states, such as Missouri and Virginia, also utilize the case-by-case approach and have stated that insurer-prescribed guidelines may be permissible, even if they materially limit the scope of representation, so long as the insured consents after consultation. See Missouri Office of Chief Disciplinary Counsel, *Informal Advisory Opinion No. 980188* (1998); Virginia Legal Ethics Opinion No. 1723 (1998). The Tennessee opinion cited above also contains language to this effect.

Two other states, Ohio and Texas, arguably follow the case-by-case approach as well, but they have condemned certain offending guidelines in emphatic terms. The Ohio Supreme Court Board of Commissioners on Grievances and Discipline, in Opinion No. 2000-3 (2000) has disallowed guidelines that provide for “demeaning” motion-by-motion evaluation of the lawyer’s work. The Board observed that “[i]f an insurer is unsatisfied with the overall legal services performed, the insurer has the opportunity in the future to retain different counsel.” The Board concluded in a more conciliatory tone, however, saying that it “encourag[ed] attorneys to cooperate with insurers, but [they] must not abdicate control of their professional judgment to non-attorneys.” The Texas Professional Ethics Committee also sounded contrasting themes – or, at least, different emphases -- in its Opinion No. 533 (2000). It began with a conventional statement that “[a]lthough the lawyer is free to enter into an agreement with the insurer regarding his fee and services to be rendered to the insured/client, such agreement cannot override the ethical responsibilities of the lawyer” But the Committee may have implied a narrow scope of permissible guidelines when it went on to say that procedures for billing and payment could be followed if they did “not [affect] the actual representation of the client.”

Finally, the Montana Supreme Court, in the previously cited *Montana Rules* case, has undertaken the sharpest critique to date of insurer-prescribed guidelines, taking particular exception to any guideline requiring “prior approval” by the insurer of certain defense services and costs. The Court held: “[D]efense counsel in Montana who submit to the requirement of prior approval violate their duties under the Rules of Professional Conduct to exercise their independent professional judgment and to give their undivided loyalty to insureds.” 2 P.3d at 817 (¶ 51). If by this holding the Montana Court meant that a lawyer could not agree to guidelines materially affecting the scope and quality of the insured’s representation – which would implicate the client’s right of informed consent and would intrude upon the lawyer’s duty to exercise independent professional judgment -- then the Court’s decision is broadly consistent with our Committee’s prior opinions and with the general pattern of opinions in other states. In fact, this reading of the Montana decision draws support from the fact that the Montana Court cited extensively the Kentucky *ALA* decision which, as mentioned earlier, approved this Committee’s Opinion E-368 (and the authorities it had cited, including Opinion E-331).

In other passages of its opinion, however, the Montana Court may have created some confusion about the dimensions of its ethical guidance to the lawyers of that state. On one hand, the Court said that its decision, adopting the one-client view of the insured/insurer/defense lawyer relationship, “should not be construed to mean that defense counsel have a ‘blank check’ to escalate litigation costs nor that defense counsel need not ever consult with insurers.” 2 P.3d at 814 (¶ 39). On the other hand, the Court also said, “Without reaching the issue here, we caution further that a mere *requirement* of consultation [with the insurer] may be indistinguishable, in its interference with a defense counsel’s exercise of independent judgment and ability to provide competent representation, from a requirement of prior approval.” 2 P.3d at 814-15 (¶ 44) (emphasis original). The Court later added that “prior approval creates a substantial appearance of impropriety in its suggestion that it is insurers rather than defense counsel who control the day to day details of a defense.” 2 P.3d at 815 (¶ 47). If by these dicta the Court was attempting to create an ethical preclusion against *any* requirement of prior “approval” regardless of the process connected with it, or against even a simple requirement of prior “consultation” with an insurer, then (and to that extent) we believe the Court’s language was overbroad and – we respectfully observe -- contrary to the better reasoned authorities.

Evidently, we are not alone in refraining from reading too much into the Montana decision. On September 8, 2000, approximately four months after the Montana Court rendered its opinion, the the

Board of Professional Responsibility of the Tennessee Supreme Court, writing *en banc* in Opinion 2000-F-145 (cited above), undertook to synthesize the ethical requirements for insurance defense lawyers. The Board, citing *In Re Petition of Youngblood*, 895 S.W.2d 322, 328 (Tenn. 1995) -- a decision quoted with approval by the Montana Court -- provided the following guidance:

The [insurer] cannot control the details of the attorney's performance, dictate the strategy or tactics employed, or limit the attorney's professional discretion with regard to the representation [quoting *Youngblood*] Counsel receiving a retention purporting to require undeviating compliance should inform the insurer that such compliance cannot be assured, but that counsel will comply to the extent permitted by counsel's duties to the insured.

It is not proper to call upon the insured to make a decision about the directives in question. ... Rather, the insured should be informed at the outset that the insurer ordinarily issues such directions. Counsel may further explain that, in light of the insurance policy and the insured's tender of defense, counsel assumes that such directions should be followed unless counsel identifies some reasonable probability that following the directive might differ from an interest of the insured.... But if counsel identifies a reasonable possibility of an interest being advanced that differs from that of the insured, counsel will consult with the insured about the decision at the time it is to be made and in light of all the circumstances then prevailing.

If this explanation is acceptable to the insured, counsel may proceed with the representation unless and until it appears that one of the directives will (or is likely to) become operative and that compliance presents a reasonable possibility of advancing an interest that differs from that of the insured.

When and if a reasonable probability becomes apparent of an interest being advanced by one of the directives that differs from that of the insured, counsel should first point this out to the insurer and inquire whether it will vary its procedure to avoid that probability. If the insurer will do so, the problem is solved and the insured protected.

If the insurer will not vary its directive, counsel must then consult with the insured. ... If the insured objects to the insurer's directive, counsel must advise the insurer that counsel cannot comply. The insurer then has a choice of accepting the insured's position, by withdrawing the objected-to directive (perhaps reserving its own right to assert that the insured has breached the policy); seeking to persuade the insured to withdraw the objection; or discharging counsel.

In no event may counsel permit the insurer's directive to cause counsel to take action -- without the insured[s] informed consent -- if counsel believes that action has a reasonable possibility of advancing an interest that would differ from that of the insured.

Like the Tennessee Board of Professional Responsibility, our Committee adheres to the widely accepted view that some insurer guidelines may be acceptable. There is no ethical (as opposed to economic) reason to condemn guidelines that standardize insurance billing practices, enhance lawyer accountability without eliminating professional judgment, require a legitimate sharing of nonconfidential information, or provide a framework for communication about the cost (and cost-effectiveness) of legal services -- not unlike the dialogue a lawyer would expect to have with a sophisticated client paying for services with first-party money. Such guidelines serve salutary purposes without infringing materially upon the attorney-client relationship. They are permissible under the case law and rules governing professional responsibility.

The guidance offered by the Tennessee Board comports well with our Committee's prior opinions, and it is broadly consistent with the Kentucky *AIA* decision mentioned above. As noted, our Supreme Court in *AIA* held that lawyers could not agree to take all of an insurance company's defense work at a fixed fee, nor could they accept such work on condition that litigation expenses would not be reimbursed. In rejecting such arrangements -- and, in a separate part of the opinion, by disallowing insurance companies to engage in the unauthorized practice of law through in-house defense counsel -- the Kentucky Court recognized that such extreme cost containment measures, to which no client had given informed consent,

nakedly pitted the economic interests of the lawyer against the insured's interest in adequate representation. Such measures purposely created a material disincentive to the exercise by counsel of independent professional judgment on behalf of clients, and *AIA* condemned them. *AIA* does not preclude less intrusive, more ethically sensitive, case handling guidelines.

An effort to develop ethically sound guidelines has been undertaken recently by the Defense Research Institute. Without pronouncing or implying any judgment on particular provisions of DRI's recommended guidelines (which can be found at the organization's Web site), our Committee notes that the proposed guidelines represent a two-year, and ongoing, collaborative project of national defense bar leaders and major insurance company representatives. Implicitly, such an effort demonstrates the view of its participants that guidelines can be crafted within ethical boundaries, and it confirms our Committee's observation in KBA Ethics Opinion E-331, quoted earlier: "Conflicts are not inevitable. Presumably these matters can be resolved amicably and responsibly in the great majority of cases."

D. Illustrative Situations

The Kentucky lawyers who requested today's opinion from our Committee have not tendered a particular set of guidelines for review, but they have raised many specific questions in addition to the broad inquiry about guidelines in general. We will consolidate and address some of those questions here. In doing so, we re-invite attention to the comments of the Tennessee Board of Professional Responsibility, quoted above, and we note the following observation of the Indiana State Bar Association Ethics Committee:

There can be no bright-line test as to the kinds of controls to which insurance defense counsel may agree. Because of the breadth of activities which a given insurer may seek to manage, the ethical propriety of a given set of guidelines is necessarily somewhat subjective. There are no better standards than those provided by Rules 5.4(c) incorporated in 1.8(f) and 1.7 (b). When confronted by proposed guidelines which cannot be followed ethically, the lawyer is well-advised to seek an acceptable modification. If such modification cannot be agreed upon, the representation must be declined. [Indiana State Bar Ethics Committee Opinion No. 3 (1998).]

We recognize that when guidelines are evaluated on a case-by-case basis, many questions will arise, not at the outset of representation -- when counsel presumably has made a threshold determination that the guidelines will be acceptable and the client has been generally informed about them -- but rather during the course of litigation. In most instances, such questions will be resolved amicably because the insurer usually shares the insured's interest in the lawyer's preparation of an effective defense.

In some circumstances, however, a disagreement may arise regarding the necessity of certain legal services as the representation unfolds. In such a situation, the lawyer may act at his or her own expense as a matter of professional duty (perhaps reserving a right on behalf of the client to seek subsequent judicial review of the insurer's decision). With the informed consent of the client, the lawyer also may perform the service in question at the client's expense or may dispense with the service if the lawyer's judgment is that the client's representation would still satisfy the basic requirement of competence under Rule 1.1. The lawyer cannot acquiesce, however, in an insurer-imposed limitation if it endangers professional competence or places other client interests significantly at risk.

A lawyer must understand that the client comes first. The lawyer prudently should decline a proffered insurance defense if it is freighted with potentially troublesome guidelines. If the lawyer agrees to guidelines that initially seem acceptable but later collide with the lawyer's independent professional judgment, and if the client does not -- and, upon consultation, should not -- consent to the limited representation, then the lawyer must protect the client by providing adequate representation regardless of the guidelines. Bearing in mind this caveat, we now turn to questions regarding particular kinds of guidelines:

1. *May a lawyer accept representation under guidelines requiring approval by the insurer (i.e., by an insurance claims adjuster) before undertaking any discovery, conducting any legal research, or filing any motion?* The question implies that the insurer would be in the position of reviewing and approving a lawyer's choice of the methods and content of discovery, or the topics and time invested in the lawyer's legal research, or the lawyer's decisions to seek rulings or relief from the court. Because each of these functions falls within the lawyer's independent professional judgment, the answer to the question is *no*. A lawyer cannot agree to representation of the insured client under guidelines that shift the exercise of professional judgment to the insurer. The lawyer could agree, however, to guidelines setting a reasonable tentative budget for these functions and providing a process for ongoing consultation if the client's interests require a budget exception.

2. *May a lawyer agree to guidelines requiring that all investigative work or all documentary review be performed only by the insurer's employees or that it be billed only at paralegal rates if performed by the lawyer's firm?* The answer is *no*. With respect to investigative work, the determination as to whether a lawyer should gain first-hand exposure to certain places, things or individuals important to the client's case, in order to prepare adequately for trial, is a matter of professional judgment. Similarly, the determination as to whether the lawyer must examine certain documents -- e.g., medical records -- directly, rather than relying upon lay or paralegal summaries, is a matter of professional judgment. Indeed, in some instances, the lawyer's first-hand review may be necessary in order to avoid potential malpractice liability. Limiting compensation for such fact-gathering or document review to paralegal rates would create a material disincentive to the lawyer's exercise of independent professional judgment, putting the client's interests at unacceptable risk. On the other hand, guidelines providing a tentative allocation of lawyer and nonlawyer/paralegal tasks appropriate to the case, or setting a reasonable tentative budget for investigative effort or document review, and providing a process for ongoing consultation, would be acceptable.

3. *May a lawyer agree to representation under guidelines requiring prior approval of compensation for additional lawyers or experts with whom the principal lawyer may wish to confer, or prior approval of compensation for a lawyer's trial preparation exceeding a specified pretrial period (e.g., thirty days)?* The answer is *yes*, if (but only if) the lawyer reasonably determines that the issues in the case do not immediately appear to require such conferences or protracted trial preparation, and that approval of additional costs can be obtained for needs becoming manifest as the case unfolds. Thus, the guidelines must provide a process for ongoing consultation with the insurer.

4. *May a lawyer agree to guidelines establishing detailed billing and reporting procedures, with deadlines for certain submissions?* The answer is *yes*, if (but only if) the guidelines contain reasonable time frames, provide a consultation process to accommodate extenuating circumstances, and do not impose upon the lawyer extreme and uncompensated time burdens that impede, or create a material disincentive to, the lawyer's performance of duties required by the attorney-client relationship. Pursuant to KBA Ethics Opinions E-404 and E-409, the lawyer also would be required to ascertain that no billing information and reports containing confidential information would go to the insurer or to outside auditors for review, without the client's informed consent.

In all of the foregoing situations, the lawyer-insurer relationship contemplates a process for ongoing consultation. Such consultation must be genuine, with the lawyer basing each expenditure or activity request on the needs of the insured, and the insurer giving each request careful consideration in light of the lawyer's independent professional judgment. If the insurer's guidelines do not provide such a process, the lawyer should decline a proffered representation. In any event, the lawyer must not undertake, and an insured client cannot be asked to accept, a representation so limited in scope that it abridges the client's rights, or narrows the lawyer's duties, under the Rules. See Comment 5 to Rule 1.2. After the representation of a client has begun -- and continuously thereafter until the representation concludes or is properly terminated under Rule 1.16 -- the lawyer must perform his or her professional duties fully, and must exercise independent professional judgment in loyalty to the client, regardless of limitations imposed by the insurer.



**PERSPECTIVES ON THE PRACTICE OF
EMPLOYMENT LAW:
THE PAST AND FUTURE**

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SECTION G



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Introduction

The 00 - "ought-ought" decade presents challenges for plaintiff employment lawyers. New technology ought to give us the tools to "level the playing field" so we can effectively combat high priced defense counsel for unreasonable employers.

Recent statistics show the number of job bias suits more than tripled from 6,936 in 1990 to 21,540 in 1998. A disturbing statistic shows that a Plaintiff in an employment case who wins in the district court is far more likely than Defendants to be reversed on appeal. The reversal rate on appeal by Plaintiff where Defendant won was 5.8%. The

* Founder of the National Employment Lawyers Association (NELA) and co-founder and former chairman of National Employee Rights Institute (now Workplace Fairness). This article is based in part upon a talk given at the ATLA National College of Advocacy and also upon an article in the NELA Employee Advocate.

reversal rate on appeal by Defendant where Plaintiff won was 53.61%.¹ The election of President George W. Bush will of course lead to the appointment of more federal judges with a pro-employer background. These new conservative judges will continue the pattern of pro-employer court rulings harmful to plaintiffs in discrimination and wrongful discharge litigation. The U.S. Supreme Court as presently constituted stands, in general, 5-4 pro-employer. Probably President Bush will have an opportunity to appoint a new conservative judge before his term expires.

It's time to look back to the 1990s.

TOP TEN EVENTS OF THE 90'S:

1. The Civil Rights Act Amendment of 1991, adding compensatory and punitive damages and jury trial for victims of race, sex, religious, and national origin discrimination, and reversing several conservative decisions of the U.S. Supreme Court.
2. The enactment of the Americans with Disabilities Act (A.D.A.) and Family Medical Leave Act (F.M.L.A.), with their protections for disabled employees and those with serious health conditions.
3. The dramatic trend of Alternative Dispute Resolution (ADR) featuring
 - a. A growing increase in management's interest in pre-suit settlement.
 - b. Corporate America's introduction of mandatory arbitration clauses in their handbooks and pre-hire employment agreements.
 - c. The increased use of mediation to help settle disputes.
4. The continued arrogance of certain companies which practice the stonewall, "deny and delay" strategy of dealing with the claims of terminated

¹ Eisenberg & Schwab "Double Standard on Appeal" <http://www.findjustice.com>.

employees. The continued use of downsizing, reorganization, and restructuring as a result of mergers and short term stock market driven decision making, which has resulted in massive layoffs.

5. The increased use of temporary and part-time employees, alleged and often misclassified independent contractors, and leased employees in order to avoid payment of fringe benefits and other liabilities.

6. The upsurge of Plaintiffs' success in sex harassment litigation and the disappointing results encountered in ERISA and ADA cases.

7. New right to privacy issues caused by increased employer monitoring of employee behavior and communications at work and off duty.

8. The slow down in expansion of common law rights and erosion of the at-will doctrine.

9. The hostile attitude of the federal bench towards employment cases, featuring increased use of summary judgment proceedings to dismiss cases.

10. The strengthening of the Plaintiffs' employment bar as exemplified by the growth of ATLA's Employee Rights Section and the National Employment Lawyers Association (NELA) and its local affiliates.

WHAT WILL HAPPEN TO THE PRACTICE OF EMPLOYMENT LAW IN THE NEXT DECADE?

1. Current ADR Trends Will Continue

There will be more mediations.

Representatives of both Plaintiffs and Defendants like mediation as a way of settling disputes. State and federal judges like to refer cases to mediation.

Administrative agencies like the EEOC, now encourage mediation. The "cottage industry" of mediators flourishes. The number of private mediations has skyrocketed. Congress, state legislators and government agencies are enacting laws and rules requiring mediations as part of the litigation dispute handling process. Companies now insert mediation as a step in their internal grievance appeal systems. Frustrated with the aggravation, delays, expenses, complexities and results of court litigation, everyone has turned to mediation as a better way to resolve disputes. This trend will continue.

There will be more pre-suit settlements by private negotiations.

The publicity concerning "ADR" and the success of mediation has forced the parties to focus on the necessity of serious exploration of "early" settlement prior to the filing of suit. In smaller cases companies are willing to analyze cost-of-defense figures and are less likely to let "machismo" and "principle" stand in the way of an expeditious, modest settlement. Employment lawyers will be doing more investigating and negotiating than ever before.

The trend towards non union "in-house" arbitration procedures will continue, albeit slowly.

The Courts should hold that 'mandatory' arbitration as a condition of employment in handbooks or employment applications is generally not "knowing and voluntary" and is therefore an invalid waiver of important statutory rights. However, any such holdings may not stop the trend of corporate America to include arbitration as the final step of internal appeal procedures. In addition, the courts tend to be yielding to public endorsement of ADR, and approving mandatory arbitration, as long as it provides minimum due process. In all events, most employees with minor claims will take

advantage of "voluntary" arbitration that is cheap, speedy and informal. However, the Plaintiffs' bar will continue to resist arbitration of major common law and statutory discrimination claims which permit trial by jury.

2. The Laws Regulating The Workforce Will Continue To Proliferate and Multiply, With Resulting Complexity and Confusion For All Concerned.

It is a certain that there will be new legislation and regulations affecting the workplace and the practice of employment law. Some of these new laws will be salutary – extending and improving protections e.g. in the field of health insurance and 401k plans. Other laws will hold the promise to the lips but will break the hearts of many because they will not live up to expectations. For certain, the complexities of the laws, the complicated interplay between federal and state law, and the complicated interplay between administrative and court law will continue to grow. For the ordinary citizen, the employment laws will often be incomprehensible and so complex as to be beyond understanding.

3. There will be no change in the "employment-at-will" doctrine and any further judicial erosion will be glacial rather than galloping.

The state courts in the late 70's and early 80's made a massive assault upon the "employment-at-will" doctrine by engrafting numerous exceptions, by extending the law of contracts (e.g. the implied employment agreement theory) and torts (e.g. the public policy tort, defamation, etc.) to the workplace. However, state courts, with a few exceptions, have been unwilling to extend the "covenant of good faith and fair dealing" and similar doctrines to the employment relationship. State courts have halted the trend

of expanding the torts of outrage and privacy which at present are of little help to employees.

Neither the state legislatures nor Congress are likely to enact legislation requiring employers to discharge employees only for "just cause". However, modern employees will not tolerate on-the-job abuse, bullying, insensitivity, unsafe unhealthy working conditions and discrimination. Employees will continue to seek remedies for unfair, discriminatory and retaliatory treatment at work.

4. The Plaintiffs' Employment Law Bar Will Continue To Grow In Numbers, Strength, and Importance.

Through publications, seminars, and other activities, ATLA and NELA do an excellent job of educating their members. The Plaintiffs' bar is now recognized in the governing councils and committees of the ABA and local bar association committees.

About ten thousand employees are terminated each day. Because of publicity and continued awareness of rights, employees continue to turn to lawyers to help them. The Plaintiffs' employment bar will continue to flourish. Million dollar verdicts will continue, although tort reform efforts will also continue to try to limit the power of juries to award large amounts of punitive damages. Big verdicts will continue to encourage settlements, which in turn will supply enough incentives for the Plaintiffs' bar to continue to represent victims of gross injustice.

Voice mail, fax, e-mail, internet and web-site communications, are helping small firm practitioners to practice law, engage in research, discovery, and trial preparation with more efficiency. Modern technology will continue to help level the playing field in the struggle between the "little guy" Plaintiff's law firm and the big Defense firm.

5. Fringe Benefit And Health Related Issues Will Continue To Be Of Importance.

Americans are more and more concerned with medical and retirement issues. The cost of health insurance continues to skyrocket. The importance of employer – sponsored welfare plans continues. There is concern and conflict with respect to new cash-balance plans, ergonomics in the workplace, managed care, ADA disability and FMLA leave of absence cases. The preemption doctrine and other defects in ERISA will continue to plague and discourage employee advocates. Recent Supreme Court decisions have further weakened the ADA as an effective instrument for disabled Americans. Undoubtedly the Enron scandal will produce some new legislation protecting employee investors in 401k Plans.

6. The Growth Of Discrimination Claims Slows Down.

The number of discrimination suits filed in the federal courts has tripled in the past decade. The Civil Rights Act Amendment of 1991 and the passage of the ADA have contributed to this growth. However, the growth trend has abated. The conservative federal bench, the difficulties of proof, the trend towards summary judgment, and the high costs of litigation have contributed to the counter trend.

7. The Ordinary Citizen Has Difficulty Finding Lawyers To Handle Modest Claims Of Injustice.

Profit minded, stock market driven corporations continue to downsize, reorganize, and restructure, causing thousands of layoffs. Companies continue to seek to eliminate older workers and those with health problems. Sex harassment and discrimination against women and minorities flourishes. Millions of victims of workplace

injustice need and will be seeking legal counsel. However, the Plaintiffs' bar is wary about accepting risky cases on a contingency fee basis. The ordinary citizen simply cannot afford hourly rate representation. The result is that thousands of injustices go unremedied. The legal system will be challenged to find new ways to provide non-contingency representation on an affordable basis.

8. New Technology Has Created Dramatic Changes In The Way Work Is Performed and In Attitudes Towards The Workplace.

The telecommuter home worker is a new phenomenon made possible by home computers. There is an increased use of independent contractors, temporary and leased employees. The new "free agent" model employee does not expect job security or have job loyalty. Concern about the right of privacy has surfaced in response to attempted corporate regulation and monitoring of electronic communications, medical records, and off duty behavior. The dramatic high speed information revolution will continue to create new legal problems in the workplace requiring new innovative legal solutions.

9. The Problem Of Employee "Consent" To "Unconscionable" Employer Policy.

Employers seek to impose mandatory arbitration of disputes on employees, and set forth arbitration rules and regulations in job applications, policy handbooks, or bilateral agreements. Frequently, employees are asked to sign statements they have read, understood and agree to obey the arbitration provision. Similarly employees sign non competition agreements upon hire and during the course of employment, and as a condition of receiving severance pay. Finally, employers more and more are issuing

announcements notifying employees that the company will be monitoring all personal e-mails and claiming implied consent to other invasions of privacy as a result of company rules in handbooks. Hopefully, the courts will examine concepts requiring “knowing and voluntary” release of statutory and contract rights and also doctrine invalidating contracts which are unconscionable, where there is an imbalance in bargaining power, the content is one-sided, and the employee is unable to understand the consequences of the so-called agreement or waiver.

10. The Major Problem Is The Failure Of The Courts To Promote The Values Of Individualism.

A gross example of the failure of the law to protect individuals in the workplace is the weakening law of privacy. Americans proclaim the importance of private matters remaining private – free from unreasonable intrusion. Yet, current laws permit companies almost unbridled freedom to drug test, monitor e-mail, search cars, lockers, desks, review medical records, and engage in surveillance and spying. Companies’ citation of the need to regulate the workforce, enforce discipline, maintain security, and prevent legal liabilities, violence, and crime is usually enough to justify almost every interference with privacy. The events of September 11, 2001, and the war on “terrorism” has encouraged employers to take more steps to monitor the workforce.

The teaching of Professor Clyde W. Summers, who recently spoke at this Institute, bears repeating:

“In [many court] cases, not only might the reasons for the discharges be viewed as “outrageous”, but the brutal way they were done should be viewed as “intolerable in a civilized society.” But the judges were unmoved. The refusal to find liability in these cases underlines the courts’ reluctance to recognize and protect employees from

egregious employer conduct which destroys their sense of self worth strips away their human dignity.

"Freedom of contract was conceived as an instrument of individualism and personal freedom, with the employment contract supposedly expressing the individual choices of the employer and employee. However, employment at will, theoretically a product of freedom of contract, is the ultimate expression of employer domination over the employee. It empowers an employer to control the employees' lives not only in their work, their dress, their speech and associations in the workplace, but also their activities and associations off the job. It empowers the employer, out of whim, vindictiveness or corrupt motives, to dismiss employees who act out of a sense of social responsibility, ethical obligation on personal conscience. To be sure, there are limits, and most employers recognize the personal worth of their employees. But courts, reasoning from employment at will, too often give little or no weight to the interests of employees. Employment at will has transformed the individualism and personal freedom into a denial of personal freedom and autonomy.

"Individualism, when expressed in terms of freedom of contract in the employment relation makes labor a commodity of trade. The individual worker becomes vulnerable to economic forces in the market where the collectivized economic power of the employer enables it to treat the worker as an object to be used, not a human being entitled to dignity, respect, individuality and autonomy.

"Employment necessarily requires some loss of individual autonomy, for the production process requires cooperation and discipline. But neither the courts nor the legislatures have reflectively sought to balance or accommodate these competing interests. Instead, they give conclusive dominant weight to the employer's interests. This invites the question why, in the employment relation, the complex of personal interests of autonomy have been given so little weight by the law in a society that prides itself on individual rights. In part, it may be that the individual's interest in autonomy is so intangible, abstract and indefinite that it is too elusive to weight, while the employer's interest in efficiency and production is tangible and visibly substantial so that its weight is obvious. But the relative weight given to these two interests may be indicative that today in our society we are

more concerned with increased production than enhancement of human worth; that what we see in the law is a reflection of ourselves; that despite our declarations of individualism, we secretly prefer products to personal autonomy."

Clyde W. Summers - - *Collectivism and Autonomy in American Labor Law* - Employee Rights and Employment Policy Journal; (2001) Volume 5; Number 2; Page 453

WHERE SHOULD THE PRACTICE OF EMPLOYMENT LAW BE GOING?

The "hope chest" of the Plaintiffs' bar.

In the recent Reeves v. Sanderson Plumbing Products, Inc., 120 S.Ct. 2097 (2000) case the U.S. Supreme Court buried the "pretext plus" doctrine once and for all and revalidated the rule that prima facie discrimination plus evidence of pretext, without more, constitutes sufficient evidence to sustain a jury verdict. Justice O'Connor writing for the majority held:

"In appropriate circumstances, the trier of fact can reasonably infer from the falsity of the explanation that the employer is dissembling to cover up a discriminatory purpose . . . Thus, a Plaintiff's prima facie case, combined with sufficient evidence to find that the employer's asserted justification is false, may permit the trier of fact to conclude that the employer unlawfully discriminated."

Hopefully the recent Eighth Circuit ruling in Mems v. St. Paul, 8th Cir. No. 99-2782 (Aug 3, 2000) is indicative of the future. There, Judge Heaney noted "Summary Judgment seldom should be granted in discrimination cases because such cases often depend on inferences rather than direct evidence." Some judges believe that employment cases unnecessarily clog the federal courts. Hopefully judicial "docket clearing" practices will now cease.

The following passage from the Third Circuit opinion in Aman v. Cort Furniture Rental Corp., 85 F.3d 1074, 1082 (1996) is appropriate.

"Discrimination continues to pollute the social and economic mainstream of American life, and is often simply masked in more subtle forms. It has become easier to coat various forms of discrimination with the appearance of propriety, or to ascribe some other less odious intention to what is in reality discriminatory behavior. In other words, while discriminatory conduct persists, violators have learned not to leave the proverbial 'smoking gun' behind. As one court has recognized, '[d]efendants of even minimal sophistication will neither admit discriminatory animus or leave a paper trail demonstrating it.' But regardless of the form that discrimination takes, the impermissible impact remains the same, and the law's prohibition remains unchanged.

"The sophisticated would-be violator has made our job a little more difficult. Courts today must be increasingly vigilant in their efforts to ensure that prohibited discrimination is not approved under the auspices of legitimate conduct, and 'a plaintiff's ability to prove discrimination indirectly, circumstantially, must not be crippled . . . because of crabbed notions of relevance or excessive mistrust of juries.'" [Citations omitted].

Hopefully the common law and legislatures of the various states will move forward to protect victims of workplace abuse. Hopefully Congress will enact the Civil Rights Tax Fairness Act to make settlements non-taxable. Hopefully Congress will modify ERISA to provide expanded remedies and modify the preemption doctrine. Hopefully the "tort reform" movement will slow down. The public needs to recognize the deterrent effect and immense social good resulting from corporate fear of jury trials and large punitive damage awards. Fulfillment of these dreams will mean a healthier environment for all employees and employment practitioners.

The fast changing times demand that the plaintiffs' bar be resilient and flexible

The changes in technology and communication featuring internet, email, voicemail, websites, cell phones, fax machines, etc., require employment lawyers to modify old methods of practice, to "work smart" and focus on efficiency. The increased use of mediation and the likely increase in arbitration will mean more cases can be handled in a much shorter time. Some lawyers will continue to "cherry pick" and select only the sure winners to litigate where large verdicts are likely after many years of litigation. However, there will be a need for more lawyers to help in the smaller cases, where the employee needs counsel to assist in company grievance procedures. There will be a continued need for counseling of employee victims of bullying, harassment, downsizing and reorganizations. Employees will continue to need help negotiating severance packages and releases. The world of employee benefits, e.g. pensions, IRA's, and medical insurance, will continue to be of great concern. Employees will be turning to lawyers more and more to unravel the complexities of benefit plans and their rights thereunder.

As the French say, "plus ca change plus c'est la meme chose", (the more something apparently changes - the more it essentially remains the same). Although the technical aspects of the Plaintiff's practice will change e.g. methods of research, use of e-mail, websites, etc., there remains the continuing need for courageous advocates who are willing to act as Davids in battle with Goliaths.

CONCLUSION

An important New York Times article by Barbara Ehrenreich is entitled "Warning: This Is A Rights-Free Work Place" and notes "Today more than ever, American workers check their freedoms at the office door. The mystery is why?" and concludes:

"What we need is nothing less than a new civil rights movement - this time, for American workers. Who will provide the leadership remains to be seen, but clearly the stakes go way beyond "labor issues," as these are conventionally defined. We can hardly call ourselves the world's pre-eminent democracy if large numbers of citizens spend half of their waking hours in what amounts, in plain terms, to a dictatorship."

The Plaintiffs' bar hopefully will be in the forefront of a new civil rights movement for American workers.

In all events, the practice of employment law continues to be exciting, interesting, and challenging and provides great opportunity for lawyers to play an important role in the community.

LITIGATION UNDER ERISA

Defense Perspective

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SECTION H



LITIGATION UNDER ERISA

Defense Perspective

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SECTION H(a)



ERISA LITIGATION

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ERISA LITIGATION

Whitney Wallingford

May 31, 2002

1. Introduction. In 1974 Congress enacted the Employee Retirement Income Security Act ("ERISA") primarily in response to growing concerns regarding the inadequate standards and safeguards then applicable to the establishment, operation and funding of employee benefit plans. ERISA §2 (29 USC §1001). Initially, ERISA's comprehensive civil enforcement scheme was intended to address issues related primarily to pension plans. Because of the increasing importance of welfare plans to employee benefit structures, the courts continue to develop and refine the rights, duties and obligations under ERISA. Basic issues which continue to be addressed include whether a jury trial may be required under ERISA, the types of damages and other remedies which are available, who has standing to sue, and what standard of review is appropriate for use by federal courts in reviewing the decisions of plan fiduciaries. ERISA's sweeping preemption provisions often result in unobtainable relief and the courts, in an attempt to remedy the inequities created by ERISA's broad preemption and limited damages provisions, are increasingly willing to create federal common law causes of action under ERISA.

ERISA litigation arises primarily in the context of enforcement proceedings, private actions brought by plan participants, beneficiaries or fiduciaries and actions brought by employees, interested parties, or the Pension Benefit Guarantee Corporation ("PBGC").

Enforcement of ERISA rights is authorized pursuant to ERISA §502 (29 USC §1132) which governs (a) persons empowered to bring a civil action, (b) actions related to qualified plans, and (c) penalties related to administrators' failure to provide information or file returns (also subject to Internal Revenue Code penalties).

2. Enforcement Proceedings

2.1 §502 of ERISA (29 USC §1132) authorizes the Secretary of Labor to investigate civil and criminal violations of ERISA and related laws and to forward violations to the Attorney General for appropriate action.

2.2 The Secretary may sue to enjoin any act or practice which violates the reporting and disclosure requirements, or the participation, vesting and funding rules of ERISA, or to obtain any other appropriate relief necessary to enforce those rules. ERISA §502(a)(5); 29 USC §1132(a)(5).

2.3 The Secretary may not bring an action for equitable relief for violation of the participation, vesting or funding rules of ERISA in the case of a qualified plan, or a plan for which an application for qualification is pending, unless requested to do so by the Secretary of the Treasury. ERISA §502(b)(1)(A); 29 USC §1132(b)(1)(A).

2.4 Participants, beneficiaries or plan fiduciaries may request that the Secretary exercise enforcement authority with regard to the participation, vesting or funding rules. ERISA §502(b)(1)(B); 29 USC §1132(b)(1)(B).

2.5 The Secretary may sue a plan fiduciary in order to secure restitution to the plan for any losses resulting from a breach of fiduciary duty and to seek the removal of the breaching fiduciary.

2.6 The PBGC has authority to make investigations and may sue in federal district court for appropriate legal and/or equitable relief in order to enforce the termination insurance provisions of ERISA. ERISA §4003; 29 USC §1303.

2.7 The Department of Labor's ("DOL") preferred method of handling ERISA violations is through voluntary compliance unless immediate action is necessary in order to preserve plan assets or to protect participants' rights.

2.8 In determining whether immediate action is necessary, the DOL will consider such factors as the flagrancy of the violation and the threat of loss of plan assets or records during the voluntary compliance period.

2.9 Judicial review of DOL regulatory actions is governed by the Administrative Procedures Act which is specifically incorporated into the labor provisions of Title I of ERISA.

2.10 Federal district courts have exclusive jurisdiction over actions for judicial review brought under Title I of ERISA. Such actions are to be brought in the district court in the district where the plan has its principal office or in the District of Columbia federal district court. ERISA §502(f), 29 USC §1132(f).

2.11 The DOL has instituted an initiative to detect "criminal activity" in ERISA plan administration. Statutes applied by the DOL include:

(a) 18 USC §664 governs theft or embezzlement from employee benefit plans. Specifically, the statute provides that:

Any person who embezzles, steals, or unlawfully and willfully abstracts or converts to his own use or to the use of another, any of the moneys, funds, securities, premiums, credits, property, or other assets of any employee welfare benefit plan or employee pension benefit plan, or of any fund connected therewith, shall be fined not more than \$10,000, or imprisoned not more than five years, or both.

As used in this section, the term "any employee welfare benefit plan or employee pension benefit plan" means any employee benefit plan subject to any provision of title I of the Employee Retirement Income Security Act of 1974.

(b) 18 USC §1027 governs false statements and concealment of facts in relation to documents required by ERISA. Specifically, the statute provides:

Whoever, in any document required by title I of the Employee Retirement Income Security Act of 1974 (as amended from time to time) to be published, or kept as part of the records of any employee welfare benefit plan or employee pension benefit plan, or certified to the administrator of any such plan, makes any false statement or representation of fact, knowing it to be false, or knowingly conceals, covers up, or fails to disclose any fact the disclosure of which is required by such title [29 USC §1001 et seq.] or is necessary to verify, explain, clarify or check for accuracy and completeness any report required by such title to be published or any information required by such title to be certified, shall be fined not more than \$10,000, or imprisoned not more than five years, or both.

(c) 18 USC §1954 governs the offer, acceptance, or solicitation to influence operations of employee benefit plans. Generally, the statute makes it a crime to accept "kickbacks" from plans.

The statute applies to anyone who is (1) an administrator, officer, trustee, custodian, counsel, agent, or employee of any employee welfare benefit plan or employee pension benefit plan; or (2) an officer, counsel, agent, or employee of an employer any of whose employees are covered by such plan; or (3) an officer, counsel, agent, or employee of an employee organization any of whose members are covered by such plan; or (4) a person who, an officer, counsel, agent, or employee of an organization which, provides benefit plan services to such plan.

Persons limited by the statute are precluded from receiving value with the intent to be influenced in their decisions. The applicable penalties are a maximum \$10,000 fine or a three year imprisonment term.

3. Private Actions

3.1 Standing to Sue

(a) Not only does ERISA §502(a) enumerate the causes of action, the statute also identifies the parties with "standing" to bring an action. The enumerated parties under ERISA §502(a) include participants, beneficiaries, fiduciaries, and the DOL.

(b) A fiduciary, plan participant or beneficiary may bring a private action under §502 of ERISA (29 USC §1132) in order to enjoin any act or practice which violates the provisions of title I of ERISA, the rules for the protection of employee benefit rights, or the terms of the plan, or in order to obtain other appropriate equitable relief to redress such violations.

(c) A civil action may be brought by a plan participant or beneficiary to recover benefits due, enforce rights under the terms of the plan, or to clarify rights to future benefits under the terms of the plan. ERISA §502(a)(1); USC §1132(a)(1).

(d) §510 of ERISA (29 USC §1140) prohibits anyone from discharging, fining, suspending, expelling, disciplining or discriminating against a participant or beneficiary for exercising rights protected by ERISA or taking part in a legal proceeding under its provisions.

(e) Outside parties who deal with an employee benefit plan do not have standing to sue to enforce their rights against the plan under ERISA.

(f) An employee benefit plan may also sue (or be sued) under title I of ERISA.

(g) Recent cases have dealt with the issue of who has standing to bring suit under ERISA.

(i) Most Circuits agree that "enumerated" parties are the exclusive parties that may sue. Whitworth Bros. Storage Co. v. Central States, Southeast and Southwest Areas Pension Fund 794 F.2d 221 (6th Cir. 1986). However, there is controversy over whether non-enumerated parties, e.g., ERISA plans, have ERISA standing.

(ii) Non-enumerated party jurisdiction may be predicated on the federal question statute (28 USC §1331). Where an action "arises under" federal common law, a federal district court may have jurisdiction over the suit. Federal courts have been authorized to evolve a federal common law of pension plans in appropriate cases. The Sixth Circuit found that preemption of state law and the congressional directive to develop a federal common law of employee benefit plans require the application of federal law to actions premised on contractual obligations created by ERISA plans. Thus, an employer could sue a plan for restitution of contributions made as the result of a mistake of law. Whitworth Bros. Storage Co. v. Central States, Southeast and Southwest Areas Pension Fund 794 F.2d 221 (6th Cir. 1986). The Sixth Circuit held that an insurance company (a non-enumerated party) had standing to bring an action for reimbursement against an ERISA-covered health plan. The court said that where the ERISA preemption provision had effectively deprived a plaintiff of a state law claim, the court had jurisdiction based on federal common law. Auto Owners Insurance Co. v. Thorn Apple Valley, Inc. 31 F.3d 371 (6th Cir. 1986), 18 EBC 1545.

(iii) At one time, the courts generally held that a plan participant who received a lump sum distribution was no longer a participant with standing to bring suit under ERISA because such a participant was no longer eligible to receive benefits under the plan. In an action by a former pension plan participant the Seventh Circuit, while holding that the participant lacked standing, stated that there was "merit to the argument that a former employee who has already received vested benefits should be allowed to bring an action within a reasonable amount of time against the administrator for failure to provide information and in order to ascertain the accuracy of the amount already received." The court, however, refused to find standing as the participant waited three years from her date of termination to file suit. Winchester v. Pension

Committee of Michael Reese Health Plan, etc., 942 F.2d 1190 (7th Cir. 1991). ERISA §502(a)(9) now makes it clear that a person who was a participant at the time of the alleged violation has standing.

(iv) The Fourth Circuit, invoking its prerogative to create federal common law under ERISA, held that the federal courts have jurisdiction over a suit brought by a plan administrator under §502(a)(1)(B) of ERISA (29 USC §1132). The court held that while §502(a)(1)(B) of ERISA provides a federal cause of action only for participants or beneficiaries, an ERISA action governed by federal common law arises under federal law where the issues in dispute are of central concern to the federal statute. Provident Life and Accident Insurance Co. v. Waller, 906 F.2d 985 (4th Cir. 1990), *cert. denied*, 111 S.Ct. 512 (1990).

(v) In Kennedy v. Connecticut General Life Ins. Co., 924 F.2d 698 (7th Cir. 1991), the court held that a health care provider has standing under ERISA to sue for benefits assigned to him by a participant in an employee welfare benefit plan. The court held that in such a situation the health care provider was a beneficiary within the meaning of ERISA.

(vi) The court in Hawaii Teamsters v. City Express Inc., 751 F. Supp. 1426 (D. Haw. 1990), held that where a union is the bargaining representative of plan participants, the union has standing to sue under ERISA to vindicate rights under the plan on behalf of its members.

3.2 Statute of Limitations

(a) ERISA does not provide a statute of limitations period for suits brought to enforce its provisions except for actions brought for breach of fiduciary duty or for actions under the special provisions relating to multi-employer plans.

(b) The controlling limitation period will be that contained in the most analogous state statute of limitations.

(c) The courts will apply the statute of limitations of the state in which the operative events relating to the cause of action occurred.

(d) An attempt by a plan to impose a shorter statute of limitations in its plan provisions may be effective if found to be reasonable. While some plan documents specify particular limitation periods in disputes, there is disagreement in the courts as to the effect of the period of limitations. Some courts suggest that the analogous state statute of limitations should be used, even though a shorter period is specified in the plan documents. Other courts have given effect to a plan document's adoption of a shorter statute of limitations. In the case of Order of United Commercial Travelers v. Wolfe, 331 U.S. 586 (1947) (a non-ERISA case), the Supreme Court upheld as valid a contract provision limiting the period of limitations, provided that the shorter period itself is a reasonable period. On the basis of Wolfe, an ERISA plan's use of a 3 year limitation for bringing a lawsuit regarding a claim was found reasonable and thus could be enforced without regard to any particular state limitation statute. Chilcote v. Blue Cross & Blue

Shield United, 841 F. Supp. 877 (E.D. Wis. 1993). See also Scheirer v. NMU Pension & Welfare Plan, 585 F. Supp. 76 (S.D. N.Y. 1984).

(e) Generally, a participant's cause of action is said to arise when the participant becomes aware of the facts necessary to state a claim, not when the participant discovers that he or she has a possible legal claim based upon those facts.

(f) According to §413 of ERISA (29 USC §1113) claims based upon a breach of fiduciary duty, absent fraud or concealment, may not be brought:

(i) more than three years after the complaining party has actual knowledge of the breach or after the filing of a report with the Secretary of Labor from which the complaining party could have reasonably been expected to obtain knowledge of the breach; or

(ii) more than six years after the date of the last action constituting a breach, or, in the case of an omission, the last date by which a fiduciary could have acted to cure the breach;

(1) Ziegler v. Connecticut Gen. Life Ins. Co., 916 F.2d 548 (9th Cir. 1990), held that not all actions for breach of fiduciary duty under ERISA require that harm occur as a result of the breach before they will accrue. The court stated that the language of §413 of ERISA clearly states that actual knowledge, and not harm, triggers the limitations period. The court applied a two part test in determining when the statute of limitations period should commence, looking first at the time that the alleged breach or violation occurred and secondly at the time that the plaintiff had actual knowledge of such breach or violation.

The court noted that to require actual harm before an action may be brought for breach of fiduciary duty would prevent the prosecution of breaches of fiduciary duty which Congress intended should be prosecuted in enacting ERISA. Such breaches include the failure to perform fiduciary duties for the exclusive benefit of participants and their beneficiaries or the transfer of plan assets to parties in interest.

(2) Another case which recognized the stringent requirement of *actual* knowledge, not merely constructive knowledge, for barring claims against fiduciaries prior to the expiration of the six year statute of limitations was Gluck v. Unisys Corp., 960 F.2d 1168, 15 EBC 1095 (3rd Cir. 1992). The court held that "actual knowledge of a breach or violation" as required under §413 of ERISA requires that a plaintiff have actual knowledge of all material facts necessary to understand that some claim exists. Such facts might include necessary opinions of experts, knowledge of a transaction's harmful consequences, or actual harm.

(iii) In the case of fraud or concealment, fiduciaries remain vulnerable to suit for a period of six years from the discovery of their breach or violation.

(1) The courts are divided as to whether the term "fraud or concealment" refers to the action giving rise to the ERISA claim or only to actions by the fiduciary to hide the breach.

(a) Radiology Center, S.C. v. Stiefel, Nicolaus & Co., 919 F.2d 1216 (7th Cir. 1990) held that the six year statute of limitations only applies to situations where a defendant fiduciary fraudulently tries to conceal an ERISA breach.

(b) Conversely, Diduck v. Kaszycki & Sons Contractors, 874 F.2d 912 (2nd Cir. 1989), held that the six year statute of limitations governs claims against trustees for breach of fiduciary duty involving fraud or concealment.

(2) Some cases have argued a concept of "ongoing breach" of fiduciary duty to avoid the limitations period. See Dameron v. Sinai Hospital of Baltimore Inc., 815 F.2d 975 (4th Cir. 1987).

(a) In Masengill v. Rye, 747 F. Supp. 362 (E.D. Ky. 1990), the plaintiffs sued for conversion of plan assets arguing that the "breach" should continue for each day the fiduciary retained control of the assets or should be said to occur each time the fiduciary refused the plaintiffs' demands for the assets. The court rejected the plaintiffs' position, holding that such an interpretation would subject fiduciaries to liability forever thereby rendering ERISA's limitation provisions meaningless.

3.3 Appeals Procedure

(a) §503 of ERISA (29 USC §1133) requires that every employee benefit plan establish special appeal procedures which provide for written notice of a claim denial to the participant or beneficiary making the claim for benefits and a reasonable opportunity for a full and fair review of the decision denying the request.

(i) Many courts require the exhaustion of interplan claim procedures as a prerequisite to bringing a suit for benefits under ERISA.

(1) In Baxter v. C.A. Muer Corp., 941 F.2d 451 (6th Cir. 1991), the court held that a plan participant who is not provided with a written denial of benefits, as required under ERISA, may still be required to appeal the claim denial before proceeding in federal court. The court held that even though a written denial of benefits was not issued, the participant, who had a copy of the plan document, was notified of the denial and could have sought review.

(2) Springer v. Wal-Mart Associates' Group Health Plan, 908 F.2d 897 (11th Cir. 1990), held that a plan administrator's refusal to process a claim did not excuse a participant from the requirement that the participant exhaust the administrative remedies available under the plan prior to filing a suit for benefits.

(ii) This prerequisite may be waived if the appeals procedures would be futile or if there has been a wrongful denial of access to such procedures.

(1) In Curry v. Contract Fabricatory, Inc. Profit Sharing Plan, 891 F.2d 842 (11th Cir. 1990), the court permitted a participant to maintain an action under ERISA for the denial of benefits despite the participant's failure to exhaust the plan's administrative remedies. The plan administrator failed to provide the participant with plan documents describing the remedies available under the plan or to document the reasons for the denial of the participant's claims. The court held that the plan administrator's actions denied the participant meaningful access to the review process and therefore exhaustion of the plan's administrative remedies was not required.

Note: In Graphic Communications v. GCIU - Employer Retirement Plan, 917 F.2d 1184 (9th Cir. 1990), the plan stated that a claim for benefits would initially be reviewed by the plan administrator whose decision could then be appealed to the fund trustees. If a participant was dissatisfied with the trustees decision, a participant could take the remaining step in the plan's administrative process which was final and binding arbitration. A participant in the plan declined to arbitrate and instead filed suit in federal district court under §502 of ERISA (29 USC §1132) contending that the arbitration provisions in the plan were unenforceable. The court held that judicial review of the benefit claim denial was unavailable due to the participant's failure to follow the plan's mandatory arbitration procedures. The court stated that arbitration clauses are unenforceable when the claim in question is one that arises under ERISA, but are enforceable where the claim involves plan interpretation. The court held that ERISA does not forbid enforcement of an agreement to arbitrate questions of coverage under ERISA plans.

(2) The Sixth Circuit has consistently followed the futility exception to the exhaustion requirement. See Fallick v. Nationwide Mutual Insurance Company, 162 F.3d 410, 22 EBC 2221 (6th Cir. 1998); Costantino v. TRW Inc., 13 F.3d 969, 17 EBC 1606 (6th Cir. 1994); see also Wilczynski v. Lumbermens Mut. Cas. Co., 93 F.3d 397 (7th Cir. 1996); Diaz v. United Agr. Employee Welfare Benefit Plan, 50 F.3d 1478 (9th Cir. 1995); Drinkwater v. Metropolitan Life Ins. Co., 846 F.2d 821 (1st Cir. 1988); Amato v. Bernard, 618 F.2d 559, 2 EBC 2536 (9th Cir. 1980); Dameron v. Sinai Hosp., 626 F. Supp. 1012, 6 EBC 2742 (D. Md. 1986), *aff'd* in pertinent part, 815 F.2d 975, 9 EBC 1246 (4th Cir. 1987).

(b) Jurisdiction

(i) Except for (a)(1)(B) actions (actions by a participant or beneficiary to recover benefits due under the terms of a plan, to enforce rights under the terms of the plan, or to clarify rights to future benefits under the terms of the plan), the federal district courts have exclusive jurisdiction over civil actions brought by participants, beneficiaries or plan fiduciaries.

(ii) The federal courts exercise concurrent jurisdiction with state courts in actions brought by participants and beneficiaries to recover benefits, enforce rights or clarify future rights. Such actions are subject to removal to federal court. Federal courts have exclusive

jurisdiction for retaliation claims under ERISA §510. Smith, Hinchman & Gryllis v. Tassic, 990 F.2d 256 (6th Cir. 1993).

(iii) Interpretation of federal courts' exclusive jurisdiction is a federal question to be decided by federal courts. Marshall v. Chase Manhattan Bank, 558 F.2d 680 (2nd Cir. 1977). Whether the matter is subject to ERISA is, however, a matter properly decided by a state tribunal. Weiner v. Blue Cross of Maryland, 925 F.2d 81 (4th Cir. 1991).

(iv) Federal courts have pendent jurisdiction over non-ERISA matters.
28 USC §1367(a).

(v) Venue for civil actions under ERISA is the place where the plan is administered, where the breach that is the subject of the suit occurred, or where the defendant resides or may be found.

(c) Venue and Nationwide Service of Process - ERISA §502(e)(2) provides that:

[W]here an action under this subchapter is brought in a district court of the United States, it may be brought in the district where the plan is administered, where the breach took place, or where a defendant resides or may be found, and process may be served in any other district where a defendant resides or may be found.

(d) Removal to Federal Court - Most state court filings can be removed to federal court because ERISA creates an independent basis for the removal (either on the basis of exclusive jurisdiction or on the basis of federal question (28 USC §1331)).

(e) Availability of Jury Trial

(i) ERISA does not expressly provide for the right to a jury trial in any of the causes of action enumerated under ERISA §502. The overwhelming weight of authority is that there is no right to a jury trial in ERISA cases. Faced with Congress' silence on the jury right issue, courts have made the determination that there is no right to a jury trial in ERISA cases because such cases are equitable in nature, since they were formerly brought under the law of trusts.

(ii) ERISA has generally been regarded as an equitable statute, and since it does not expressly provide for jury trials, the Seventh Amendment's right to a jury trial has generally been held not to apply to ERISA actions. However, two U.S. Supreme Court cases had indicated that remedies other than equitable ones may be available under ERISA. In Firestone Tire and Rubber Co. v. Bruch, 109 S.Ct. 948 (1989), the Court compared benefit claims to breach of contract actions which are legal in nature, and in Ingersoll-Rand Co. v. McClendon, 111 S.Ct. 478 (1990), the Court indicated that compensatory damages, a legal remedy, are within the scope of ERISA. In light of these developments, courts need to re-examine the issue of the right to a

jury trial under ERISA. As a result of the Supreme Court's decision in Mertens v. Hewitt Associates, 113 S.Ct. 2063, 16 EBC 2169 (1993), it appears that jury trials are not authorized.

(iii) In Vicinanzo v. Brunswick & Pils Inc., 739 F. Supp. 882 (S.D.N.Y. 1990), the court held that the right to a jury trial guaranteed under the Seventh Amendment applies to actions under §510 of ERISA, which prohibits discrimination against a plan participant or beneficiary for the exercise of rights under ERISA.

(iv) In McDonald v. Artcraft Electric Supply Company, 774 F. Supp. 29 (D.D.C. 1991), the court held that plaintiffs seeking damages under ERISA have a right to a jury trial both under ERISA and the Seventh Amendment. The court held that the Seventh Amendment applies when a statutory right is based on a legal cause of action and traditional legal relief is available under the statute. Therefore, the Seventh Amendment gives parties the right to a jury trial when they bring claims under ERISA that would have entitled them to a jury trial had they been brought under state law prior to ERISA.

4. ERISA Preemption

4.1 Statutory Framework

(a) Preemption clause - ERISA §514(a) provides that ERISA supersedes state laws "insofar as they may now or hereafter relate to any employee benefit plan. . . ." The Supreme Court has held that the phrase "relate to" should be given a broad common-sense meaning, "such that a state law 'relate[s] to' a benefit plan 'in the normal sense of the phrase, if it has a connection with or reference to such a plan'." See Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724, 739, 105 S. Ct. 2380, 2389 (1985) (quoting Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 97 (1983)). In fact, the Court has stated that the preemption clause was designed to displace all state laws falling within its scope, even laws that mirror ERISA's substantive provisions. Id., 105 S. Ct. at 2389 (citing Shaw, 463 U.S. at 98-99). The Court has emphasized, however, "that the pre-emption clause is not limited to 'state laws specifically designed to affect employee benefit plans.'" See Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 47-48, 107 S. Ct. 1549, 1553 (1987) (quoting Shaw, 463 U.S. at 98). This broad interpretation of the preemption clause is consistent with the legislative history of the statute, and the Supreme Court has noted that congressional purpose is the "ultimate touchstone" in determining whether a state law is preempted by federal law. Id. at 45, 107 S. Ct. at 1552.

(b) Savings clause - ERISA §514(b) permits states to regulate insurance, banking and securities. The preemption clause is qualified by §514(b)(2)(A) of ERISA. That section, known as the "saving clause," provides, "Except as provided in subparagraph (B), nothing in this title shall be construed to exempt or relieve any person from any law of any state which regulates insurance . . ." 29 USC §1144(b)(2)(A). For a state law to be "saved" from the application of the preemption clause, it must, according to the Supreme Court, pass a test which may, depending on the facts of the case, have two parts. The first prong of the test, which is present in every case, is whether a law "regulates insurance." To determine whether a law regulates insurance, the Supreme Court has devised a two-step test. First, it asks whether the statute in question regulates insurance from a "common-sense view." See Pilot Life Ins. Co. v.

Dedeaux, 481 U.S. 41, 48, 107 S. Ct. 1549, 1553 (1987). To pass this test, "a law must not just have an impact on the insurance industry, but must be specifically directed toward that industry." See id. at 50, 107 S. Ct. at 1554. The second part of the "regulates insurance" test asks whether the law at issue meets certain criteria used to determine whether a particular practice falls within the McCarran-Ferguson Act's reference to the "business of insurance." Those criteria are: "[F]irst, whether the practice has the effect of transferring or spreading a policyholder's risk; second, whether the practice is an integral part of the policy relationship between the insurer and the insured; and third, whether the practice is limited to entities within the insurance industry." See Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724, 743, 105 S. Ct. 2380, 2391 (1985) (quoting Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 129, 102 S. Ct. 3002, 3008 (1982)) (emphasis in original). If a state law passes both the "common-sense" and the McCarran-Ferguson tests, it will fall under the "regulates insurance" language of the saving clause.

Even if the state law passes the "regulat[ing] insurance" hurdle, it still might not be held to be saved from preemption. In Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 52, 107 S. Ct. 1549, 1555 (1987), the Court found that because "the state cause of action seeks remedies for the improper processing of a claim for benefits under an ERISA-regulated plan, our understanding of the saving clause must be informed by the legislative intent concerning the civil enforcement provisions provided by ERISA §502(a), 29 USC §1132(a)." In other words, where the state law at issue is remedial in nature, the Court found that it had to consider not only the tests for meeting the "regulates insurance" language of the saving clause, "but also the role of the saving clause in ERISA as a whole." See id. at 51, 107 S. Ct. at 1555. The Court in Pilot found that the civil enforcement scheme set forth in §502(a) was intended to be the exclusive remedy for asserting improper processing of claims, and that this exclusivity would be undermined if ERISA-plan participants and beneficiaries could obtain relief under varying state law remedies that were rejected by Congress when it crafted ERISA. In holding that the state law cause of action for improper processing of an insurance claim was not saved by the saving clause, and was therefore preempted by the preemption clause, the Court noted that the most important factor in its decision was Congress' intent that ERISA's civil enforcement provision be exclusive. See id. at 52, 54, 57, 107 S. Ct. at 1555-56, 1558. Consequently, in cases where the state law in question might affect the remedies section of ERISA, it is not enough that the state law meets the "regulating insurance" test; it must also pass the "role-of-the-saving-clause-in-ERISA-as-a-whole" test.

In UNUM v. Ward, 526 US 358, 22 EBC 2745(1999), the U.S. Supreme Court upheld the 9th Circuit holding that California's "notice-prejudice" rule regulated insurance and was thus "saved" from preemption by ERISA. Here, the state law required that "[A] defense based on an insured's failure to give timely notice [of a claim] requires the insurer to prove that it suffered actual prejudice. Prejudice is not presumed from delayed notice alone. The insurer must show actual prejudice, not the mere possibility of prejudice." ERISA did, however, preempt the California rule that the employer is the agent of the insurer.

(c) Deemer clause - ERISA §514(b)(2)(B) precludes a state from "deeming" a plan to be an insurance company, bank, etc. for purposes of bringing it under state regulation. Even if a state law meets all the applicable requirements of the saving clause test, it still may be preempted by virtue of §514(b)(2)(B) of ERISA, known as the deemer clause. That clause provides:

Neither an employee benefit plan described in §4(a) [29 USC §1003(a)], which is not exempt under §4(b) [29 USCS §1003(b)] (other than a plan established primarily for the purpose of providing death benefits), nor any trust established under such a plan, shall be deemed to be an insurance company or other insurer . . . or to be engaged in the business of insurance . . . for purposes of any law of any State purporting to regulate insurance companies . . . [or] insurance contracts 29 USC §1144(b)(2)(B).

The Supreme Court has interpreted the effect of the deemer clause: "If a plan is insured, a State may regulate it indirectly through regulation of its insurer and its insurer's insurance contracts; if the plan is uninsured, the State may not regulate it." See F.C. Corp. v. Holliday, 111 S. Ct. 403, 411 (1990). An uninsured or self-insured plan is one which "set[s] aside a fund to meet losses instead of insuring against such through insurance." Black's Law Dictionary 1360 (6th ed. 1990). As a result of the Court's holding in F.C., employers attempting to implement self-insured plans affecting employees in different states should not have to confront "conflicting or inconsistent State and local regulation of employee benefit plans." F.C. Corp., 111 S. Ct. at 411 (quoting Shaw v. Delta Air Lines, Inc., 463 U.S. 85, 99, 103 S. Ct. 2890, 2901 (1983) (quoting remarks of Sen. Williams)).

4.2 Application to Health Insurance Arrangements

One of the landmark cases that dealt directly with health insurance arrangements was Metropolitan Life Ins. Co. v. Massachusetts, 471 U.S. 724, 105 S. Ct. 2380 (1985). In that case, the Court considered whether a Massachusetts statute, which required minimum mental health benefits be provided to Massachusetts residents who were insured under a general insurance policy, an accident or sickness policy, or an employee health-care plan covering hospital and surgical expenses, was preempted by ERISA. Because the Attorney General of Massachusetts found that appellant insurers Metropolitan Life Insurance Company and Travelers Insurance Company were issuing policies outside of Massachusetts which failed to provide the requisite mental health coverage mandated by the statute, and because the insurance companies reserved the right to challenge the applicability of the statute to any policy they issued to an ERISA plan within Massachusetts, he brought suit for declaratory and injunctive relief to enforce the statute. The insurers asserted, *inter alia*, that the mandated-benefits statute was preempted by ERISA, while Massachusetts argued that the statute, as applied to insurance companies that sell insurance to ERISA plans, was a law regulating insurance and was thereby saved by virtue of the saving clause from the operation of the preemption clause. See *id.* at 733-34, 105 S. Ct. at 2385-86. The Court noted that the Supreme Judicial Court of Massachusetts had found that the statute related to a benefit plan and thus would be preempted by ERISA unless it fell under one of the exceptions to the preemption clause. The lower court found that the statute was a law which regulated insurance and therefore was not preempted by ERISA. It rejected the insurers' claim that the saving clause was intended only to save "traditional" insurance laws (such as laws directly regulating insurers and laws regulating such matters as the way insurance may be sold), finding no such limitation in ERISA's language. In so finding, however, the lower court understood the saving clause to apply only to state laws that were unrelated to ERISA's substantive provisions. Because ERISA did not regulate the content of welfare plans, the court declared that state regulation of insurance that indirectly affected the content of the plans themselves was not preempted by ERISA. Further, the lower court held that the McCarran-Ferguson Act embodied Congress' intent that federal laws

should not be found to supersede state laws regulating the business of insurance. Because the statute in question affected insurance and insurance policies, the court found that it was protected by the McCarran-Ferguson Act and that therefore it was not preempted by ERISA. See *id.* at 735-37, 741, 105 S. Ct. at 2387, 2390.

The Court affirmed the lower court's ruling, although it employed a broader reading of the saving clause. See *id.* at 758, 105 S. Ct. at 2399. In arriving at its ultimate holding that the statute was not preempted by ERISA, the Court first examined whether the statute was related to ERISA within the meaning of the preemption clause. Noting that the phrase "relate to" was to be given a broad reading, the Court found that although the statute was not designated as a benefit plan law, it bore indirectly on but significantly affected all insured ERISA plans, because it required them to purchase the mandated benefits specified in the statute when they purchased certain kinds of insurance policies. Thus, the Court agreed with the lower court that the statute related to ERISA plans and thus fell within the preemption clause. See *id.* at 739, 105 S. Ct. at 2388-89.

The Court found that the saving clause saved the statute from preemption. See *id.* at 744, 105 S.Ct. at 2391. In arriving at its conclusion, the Court first examined the statute from a common-sense point of view. It noted that because on its face the statute regulated the terms of certain insurance contracts, it seemed to be saved from preemption by operation of the saving clause as a law which regulated insurance. See *id.* at 740, 105 S.Ct. at 2389. The Court stated that its interpretation was reinforced by the deemer clause, which provides that a plan "shall not be deemed to be an insurance company 'for purposes of any law of any State purporting to regulate insurance companies . . . [or] insurance contracts'" *Id.* at 740-41, 105 S. Ct. at 2389 (quoting 29 USC §1144(b)(2)(B)) (emphasis in original).

The Court then turned to the question of whether the statute met the criteria for defining the business of insurance under the McCarran-Ferguson Act. As to the first factor, the Court found that the statute effected the spreading of risk, as it was enacted to spread the risk of mental health patients through more risk pools. Second, the Court found that the statute regulated an integral part of the policy relationship between the insurer and the insured by defining the type of insurance that an insurer could sell. Finally, the Court found that the practice was limited to entities within the insurance industry, as the mandated-benefit law imposed its requirements only on insurers. In light of the fact that the statute met the common-sense definition of regulating insurance and all three McCarran-Ferguson factors, the Court held that mandated-benefit statutes such as the one in question were saved from the preemption clause by virtue of the saving clause. See *id.* at 743-44, 105 S. Ct. at 2391.

The Court expanded on its analysis of the saving clause in Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 107 S. Ct. 1549 (1987). In Pilot, Dedeaux, an employee of Entex, Inc. ("Entex"), injured his back in an employment related accident. Entex had in place a disability benefit plan which it established by purchasing a group insurance policy from Pilot Life Insurance Co. ("Pilot Life"). Dedeaux sought permanent disability benefits following his accident, but Pilot Life terminated his benefits two years after the accident. Subsequently, Pilot Life reinstated and terminated Dedeaux's benefits several times. Five years after the accident, Dedeaux sued Pilot Life for tortious breach of contract, breach of fiduciary duties, and fraud in the inducement. Pilot Life argued that Dedeaux's claims were preempted under ERISA, and the district court agreed,

granting Pilot Life's motion for summary judgment. The Fifth Circuit reversed. *Id.* at 43-44, 107 S. Ct. at 1551. The Supreme Court reversed the holding of the Fifth Circuit. *Id.*, 107 S. Ct. at 1551. The Court quickly dispatched of the question of whether the common law causes of action related to an employee benefit plan; it held that they did. See *id.* at 47-48, 107 S. Ct. at 1553. The Court next turned to the question of whether the saving clause saved Dedeaux's cause of action for tortious breach of contract/bad faith. The Court found that the cause of action for bad faith did not meet the common-sense prong of the regulating insurance test. See *id.* at 48, 107 S. Ct. at 1553. The Court stated that in order for a law to regulate insurance, it "must not just have an impact on the insurance industry, but must be specifically directed toward that industry." *Id.* at 50, 107 S. Ct. at 1554. Noting that the Mississippi Supreme Court had identified the law of bad faith with the insurance industry, the Court nevertheless held that the foundation of the law could be found in general principles of tort and contract law. Further, the Court found that the McCarran-Ferguson Act factors did not support Dedeaux's claim that the bad faith law regulated insurance. The Mississippi common law of bad faith could not be said to effect a spreading of policyholder risk, the Court noted, nor could it be said under the third factor that the law was specifically directed towards entities within the insurance industry, as the law of bad faith had derived from general principles of tort and contract law. Although the Court acknowledged that the common law of bad faith could be construed to concern the policy relationship between the insurer and the insured, it found that the relationship was tenuous. See *id.* at 50-51, 107 S. Ct. at 1554-55.

The Court went on to state that it had to be guided not only by the factors it considered in Metropolitan Life, but also by "the role of the saving clause in ERISA as a whole." *Id.*, 107 S. Ct. at 1555. The Court noted that in this case, unlike Metropolitan Life, the plaintiff was seeking remedies for improper processing of a benefits claim, and therefore the court had to consider the civil enforcement provisions of ERISA. The Court found that the civil enforcement provisions of ERISA were intended to be the exclusive means by which ERISA-plan participants and beneficiaries asserting improper processing of a claim for benefits could recover, based on the language and structure of the statute and the legislative history of the statute. See *id.* at 51-52, 107 S. Ct. at 1555. Thus, the Court held that based on the common-sense and the McCarran-Ferguson prongs of the regulating insurance test and the congressional intent that ERISA's civil enforcement provisions be exclusive, the common law cause of action for bad faith was preempted by ERISA. See *id.* at 57, 107 S. Ct. at 1558.

After the Court's decision in Pilot Life, a question that many of the lower courts addressed was whether a statutory claim for improper handling of claims/unfair settlement practices would survive the preemption analysis laid down in Pilot Life. For example, one court addressed the issue of whether a statutory cause of action under the California insurance code for failure to pay claims promptly was preempted by ERISA. See Kanne v. Connecticut Gen. Life Ins. Co., 867 F.2d 489 (9th Cir. 1988), *cert. denied*, 492 U.S. 906 (1989). The Kannes sought reimbursement for airline fare to transport their son for surgery, as well as compensation for emotional distress caused by the delay in payments for the airline, doctor, and hospital bills. The lower court had awarded the Kannes over \$750,000 in compensatory and punitive damages. *Id.* at 491. The court noted that California Insurance Code §790.03(h) prohibited unfair insurance practices with respect to the processing of claims. Among the unfair practices listed in the statute was an insurer's failure "to acknowledge and act reasonably promptly upon communications with respect to claims

arising under insurance policies." *Id.* at 493 (quoting Cal. Ins. Code §790.03(h)(2)). The Kannes argued that the statute was not preempted by ERISA because it was saved as a law regulating insurance. The court granted them the assumption that the statute was a law regulating insurance within the meaning of the saving clause. Nevertheless, the court decided that the private right of action for violation of the statute was preempted by ERISA. *Id.*

In deciding that the California statute was preempted, the court noted that the Supreme Court "made [it] abundantly clear that its preemption holding [in Pilot Life] was equally based [on the regulation of insurance test and] on its acceptance of the Solicitor General's view that 'Congress had clearly expressed an intent that the civil enforcement provisions of ERISA §502(a) be the exclusive vehicle for actions by ERISA-plan participants and beneficiaries asserting improper processing of a claim for benefits.'" *Id.* at 494 (quoting Pilot Life, 107 S. Ct. at 1555). In interpreting the Supreme Court's language, the court held that it could not allow a state statute like the one in question to supplement the ERISA civil enforcement provisions. As a result, the court found that the Kannes' statutory cause of action for failure to pay claims promptly was preempted.

Further, the decision of the Court in Pilot Life has been extended to preempt a state common law holding that an insurer of a group employment health plan was required to notify plan participants of the cancellation or modification of the insurance policy caused by failure of the employer to pay the insurance premiums. See Presley v. Blue Cross-Blue Shield of Alabama, 744 F. Supp. 1051 (N.D. Ala. 1990).

4.3 Application to Professional Negligence Claims

(a) As a general rule, courts will not find that ERISA preempts state law claims based upon negligence or malpractice. This appears to hold true for claims against physicians (DeGenova v. Ansel, 555 A.2d 147, 150 (Pa. Super. 1988) (malpractice claim for personal injuries "only remotely related to ERISA" and therefore not preempted)), accountants and actuaries (Framingham Union Hosp., Inc. v. The Travelers Ins. Co., 721 F. Supp. 1478, 1490 (D. Mass. 1989) (malpractice claim against accountant not preempted)); and legal counsel (Custer v. Sweeney, 89 F.3d 1156, 20 EBC 1569 (4th Cir. 1996)).

(b) In addressing the application of the preemption doctrine to medical malpractice cases, the courts continue to be confronted and struggle with the notion of the relationship of the law at issue and the benefit plan. Some courts have decided that medical malpractice claims are preempted. For example, the Eighth Circuit in Hull v. Fallon, 188 F.3d 939, 23 EBC 2062 (8th Cir. 1999), *cert. denied*, 120 S.Ct. 1242, 23 EBC 3016 (2000), held preempted claims against a plan's administrator for medical malpractice arising from the administrator's alleged failure to exercise a sufficient degree of care in diagnosing and treating a participant and for vicarious liability of the plan. The primary care physician of the participant twice requested authorization for a particular test. The physician's requests were denied by the plan's administrator. Instead the administrator, a physician, authorized a different test. The participant claimed that as a result of the plan administrator's action, he suffered additional heart disease. He claimed a doctor-patient relationship between himself and the plan administrator. The court determined that the participant's claims were based on a denial of benefits. Because the

claims related to the administration of benefits, the court concluded, they were preempted. See also Jass v. Prudential Health Care Plan, Inc., 88 F.3d 1482, 20 EBC 1580 (7th Cir. 1996), and Kuhl v. Lincoln Nat'l Health Plan of Kansas City, Inc., 999 F.2d 298, 16 EBC 2745 (8th Cir. 1993).

Recent cases holding that ERISA preempts medical malpractice claims include:

(i) Kuhl v. Lincoln National Health Plan, 992 F.2d 298, 16 EBC 2745 (8th Cir. 1993), *cert. denied*, 114 S. Ct. 694 (1994), involving a claim against an HMO for denying surgical precertification preempted by ERISA;

(ii) Corcoran v. United Healthcare, Inc., 965 F.2d 1321, 15 EBC 1793 (1993), *cert. denied*, 113 S.Ct. 812 (1992), involving the preemption of a claim against an HMO for failure to provide hospitalization to expectant mother resulting in death of unborn child; and

(iii) Papas v. Asbel, 675 A.2d 711, 20 EBC 1106 (Sup. Ct. Pa. 1996), refusing to apply preemption in a case where a medical facility failed to timely transfer a patient. Here the court looked at the economic interest of the entity.

5. Fiduciary Liability

5.1 Under ERISA a plan fiduciary is liable for breaches of fiduciary duty. ERISA §§409 and 502(a)(2). Liability does not exist, however, for "settlor functions."

5.2 A person is a fiduciary of an employee benefit plan to the extent that the person: (1) exercises discretionary authority or control respecting management of such plan or management or disposition of its assets; (2) renders or has authority or responsibility to render investment advice for a fee; or (3) has discretionary authority or responsibility in the administration of such plan. ERISA §3(21)(A).

5.3 Settlor Functions

(a) A plan sponsor may amend the terms of a plan to provide encouragement for early retirement, and in so doing is acting in a settlor function. Lockheed Corporation v. Spink, 517 U.S. 882 (1996).

(b) Spink was recently reaffirmed by the Supreme Court in Hughes Aircraft v. Jacobson, 525 U.S. 432 (1999), where the amendment of a plan was intended to convert the benefit structure of a defined benefit plan and to add a contributory component.

(c) In certain cases, HMO eligibility decisions have been held to be non-fiduciary in nature. Pegram v. Hendrick, 120 S. Ct. 2143, 24 EBC 1641 (2000).

(d) The Third Circuit held that the imposition of a penalty on a plan participant who failed to obtain precertification approval as required by the plan prior to his hospitalization was not an action subject to ERISA's fiduciary responsibility rules as an employer has no fiduciary

liability for design decisions that it makes with respect to its employee benefit plans. Nazay v. Miller, 949 F.2d 1323 (3rd Cir. 1991)

(e) In Owens v. Storehouse, Inc., 773 F. Supp. 416 (N.D. Ga. 1991), the District Court held that an employer serving as the plan administrator of its self-insured medical plan did not breach ERISA's fiduciary responsibility rules by unilaterally reducing the lifetime coverage limit from \$1 million to \$25,000. A plan participant with AIDS challenged the reduction, but the Court held that the employer was not prohibited from "acting in accordance with its interests as an employer when not administering the plan or investing its assets." The court further held that the reduction was permissible as ERISA's fiduciary responsibility rules do not apply to the elimination of non-vested benefits.

(f) The court in Bryant v. Food Lion Inc., 774 F. Supp. 1484 (D.S.C. 1991), held that corporate officers do not breach their fiduciary duty by utilizing a permissible graded vesting schedule which results in only a small fraction of employees becoming vested in their accrued benefits due to high employee turnover. The court held that the selection of a permissible vesting schedule was a design decision made by the employer and was not subject to ERISA's fiduciary responsibility rules.

(g) In Carich v. James River Corp., 958 F.2d. 861 (9th Cir. 1992), a plan administrator and fiduciary was held to have breached its fiduciary obligations under ERISA due to the employer's unreasonable delay in transferring a plan participant's plan assets from one investment fund to another. The court held that authorization in the plan to value stock as of the date of sale, regardless of any delay resulting from improper handling, gave the plan and its administrator unlimited discretion in the handling of fund transfers which was contrary to the principles underlying ERISA. The court held that in the absence of notice to the participant concerning the likelihood of delay, the participant was entitled to have the transfer made as of the date requested, or at least within a reasonable time following such request. The employer's failure to act with due diligence was held to be arbitrary and capricious and in violation of its contractual obligations to the participant. The court held that any risk of unreasonable delay due to the administration of the plan was a risk to be borne by the employer, and not by the plan participants.

(h) Insurers as Fiduciaries

(i) In Mack Boring & Parts v. Meeker Sharkey Moffitt, Actuarial Consultants of New Jersey, 930 F.2d 267 (3d Cir. 1991), the Third Circuit held that an insurance company was not a plan fiduciary within the meaning of ERISA where the insurer entered into a deposit authorization contract with an employer to fund the employer's defined benefit plan. The contract provided for the employer to make annual contributions to the insurer in the form of premiums which were credited to a "guaranteed fund account." This fund was a bookkeeping device in which interest was credited at a guaranteed minimum rate with the possibility of higher returns at the discretion of the insurer. The premium payments were held as part of the insurer's general assets and when a plan participant retired, the insurer issued a guaranteed annuity pursuant to the terms of the plan. The cost of the annuity was then deducted from the guaranteed fund account. The court concluded that the deposit authorization contract was a guaranteed benefit policy because the contract provided benefits to participants, the amount of which were guaranteed

by the insurer in the form of an annuity. Since §401(b)(2) of ERISA (29 USC §1101) states that amounts paid by a plan to an insurer under a guaranteed benefit policy are not considered plan assets, the court held that the insurer was not a plan fiduciary as it did not have discretionary authority or control over plan assets.

In reaching this conclusion the Third Circuit rejected the Seventh Circuit's analysis in Peoria Union Stock Yard Co. Retirement Plan v. Penn. Mut. Life Ins. Co., 698 F.2d 320 (7th Cir. 1983), in which the Seventh Circuit held that a similar contract was comprised of two phases: an accumulation phase, during which premium payments were held by the insurer in its general account for investment purposes; and a payment phase, during which the insurer made payments to plan participants in the form of annuities upon retirement. The Seventh Circuit concluded that the contract was not a guaranteed benefit policy since the premiums paid to the insurance company during the accumulation phase were not used to provide "benefits, the amount of which is guaranteed by the insurer," as required by the §401(b)(2) (29 USC §1101) exception.

The Third Circuit concluded that such contracts do not fail to satisfy the guaranteed benefit policy exception merely because the benefits provided under the contract are not delivered immediately. The court stated that the variable interest credited to the guaranteed fund does not vary benefits payable to participants, but merely shifts a portion of the investment risk from the insurer to the employer. The Third Circuit's holding suggests that the investment component of such contracts are irrelevant if the insurer guarantees the participants' benefits, regardless of the amount of control the insurer exercises over the amounts available to pay such benefits.

5.4 In Varity Corporation v. Howe, 516 U.S. 489 (1996), the Supreme Court held that representations of financial condition of a plan were administrative in nature, and the employer was acting in a fiduciary capacity rather than a settlor.

5.5 Liability of Non-Fiduciary - Mertens

In a decision that has profound implications impacting liability for ERISA non-fiduciary service providers, the Supreme Court held in Mertens v. Hewitt Associates, 113 S.Ct 2063, 16 EBC 2169 (1993) that "appropriate equitable relief" within the meaning of §502(a)(3) of ERISA does not include a claim for money damages against a non-fiduciary. It is also implied in the decision that there is no cause of action against a non-fiduciary under ERISA §502(a)(3), or by analogy under §502(a)(5), for a claim of knowing participation in a fiduciary breach.

In Mertens the plaintiff, a plan beneficiary, alleged that the plan's actuarial consultant (Hewitt), had knowingly participated in the plan sponsor's fiduciary breach of deliberately failing to adequately fund the plan. The primary breach resulted from the use of actuarial assumptions that ultimately resulted in under-funding as well as a failure to disclose the under-funding. At the time of suit, the plan had been terminated and taken over by the PBGC. Because of PBGC limitation on insured benefits, the plan payments were less than pre-termination payments or payment promises. Despite styling the damages as restitution, the plaintiff sought monetary damages sufficient to restore the plan's funded status to what it would have been absent the breach.

Framed in simple terms, the plaintiff was seeking to impose monetary liability against a non-fiduciary for knowingly participating in a fiduciary breach. The case was initially dismissed by the Northern California federal district court, and the dismissal was upheld by the Ninth Circuit.

In the Supreme Court the plaintiff sought to argue that the damages were, in effect "appropriate equitable relief" under ERISA §502(a)(3). Noting that monetary damages represent the "classic form of legal relief," the Court affirmed the Ninth Circuit.

In the wake of Mertens a number of lawsuits for money damages against non-fiduciaries were dismissed. At the same time, suits brought against non-fiduciaries seeking equitable relief (e.g., restitution to the plan) have been able to survive dismissal, because Mertens did not rule out such relief. In Reich v. Compton, 834 F. Supp. 743, 17 EBC 1321 (E.D. Pa.), a suit for damages brought by the DOL against a non-fiduciary engaged in transactions with ERISA plans was dismissed in light of Mertens.

In Reich v. Rowe, 20 F.3d 25, 17 EBC 2521 (1st Cir. 1994), the First Circuit contrasted actions against non-fiduciaries alleging participation in a fiduciary's breach with actions against non-fiduciary parties in interest alleging participation in prohibited transactions. According to the court, transactions prohibited under ERISA §406 constitute acts or practices for which ERISA §502(a)(5) provides a remedy.

In Harris Trust and Savings Bank v. Salomon Smith Barney, 120 S. Ct. 2180, 24 EBC 1654 (2000), the Supreme Court, in a unanimous decision, adopted the position that ERISA §502(a)(3), and the similarly worded ERISA §502(a)(5), authorizes a civil action against a non-fiduciary who participates in a transaction prohibited by ERISA.

6. Standard of Review

6.1 The Supreme Court addressed the issue of the proper standard of review which should be applied with respect to the denial of benefit claims in Firestone v. Bruch, 489 U.S. 101 (1989). The Court held that a denial of benefits which is challenged under §502(a)(1)(B) of ERISA (29 USC §1132(a)(1)(B)) should be reviewed under a de novo standard unless the plan gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan. However, the Court held that if the administrator or fiduciary is operating under a conflict of interest, the conflict must be weighed as a factor in determining whether an abuse of discretion has occurred.

(a) The courts in applying and interpreting Firestone have generally been unable to agree on the degree of specificity necessary in the plan language to confer sufficient discretion to insure review under an arbitrary and capricious standard. In many cases, language conferring discretion on plan administrators and trustees to "construe and interpret" the plan has been deemed sufficient. See Fuller v. CBT Corp., 905 F.2d 1055 (7th Cir. 1990); DeWitt v. State Farm Ins. Co. Ret. Plan, 905 F.2d 798 (4th Cir. 1990). Other courts have required an unambiguous authorization of discretion with respect to the specific issue before the court. See e.g., Baxter v. Lynn, 886 F.2d 182 (8th Cir. 1989). In Baxter the plan stated that the trustees had

"final authority" to determine all matters of eligibility for the payment of claims. The Eighth Circuit held that such language did not grant the discretionary authority necessary within the meaning of Firestone to interpret ambiguous plan terms, and therefore a *de novo* standard of review should be applied.

(b) The court in Firestone did not clearly define the meaning of *de novo* review or the extent to which evidence not presented to plan administrators must be considered.

(i) In Perry v. Simplicity Eng'g, 900 F.2d 963 (6th Cir. 1990) the court interpreted Firestone narrowly and limited *de novo* review to the evidence before the plan administrator. The Sixth Circuit stated that a primary goal of ERISA was to provide for the inexpensive and expeditious resolution of disputes concerning benefits, and that permitting courts to hear evidence not presented to plan administrators will result in employees and their beneficiaries receiving less protection than Congress intended.

(ii) However, in Moon v. American Home Assurance Co., 888 F.2d 86 (11th Cir. 1989), the Eleventh Circuit held that Firestone permits a court conducting a *de novo* review to consider facts not available to the plan administrator at the time the final determination was made. According to the court, restricting the facts on review to only those which were available to the plan administrator would afford less protection to employees and their beneficiaries than existed before the enactment of ERISA.

(c) There is a split among the Circuits as to whether a plan administrator's factual, as well as interpretive, determinations are subject to *de novo* review.

(i) The Third Circuit in Luby v. Teamsters Health, Welfare, and Pension Trust Funds, 944 F.2d 1176 (3d Cir. 1991), held that the *de novo* standard of review should be applied to a plan administrator's fact-based determinations where the plan does not confer authority on the plan administrator to decide disputes between beneficiary claimants or require deference to the plan administrator's factual determinations. The court stated that the factual determinations of a plan administrator should not be given deference due to the fact that plan administrators are often lay persons who lack training, experience, or an understanding of ERISA, the rules of evidence, or the legal procedures necessary to assist them in fact finding.

(ii) In contrast, the Fifth Circuit in Pierre v. Connecticut General Life Ins. Co., 932 F.2d 1552 (5th Cir. 1991), held that the *de novo* standard of review applies only to instances of plan interpretation in which the facts are not in dispute, and that a plan administrator's factual determinations in such a situation should be entitled to deference. According to the court, the discretion to make factual determinations is inherent in the nature of the plan administrator's job and, unlike the Third Circuit, the court believed that plan administrators are qualified to make such factual determinations.

(iii) The Second Circuit has held that even where it is undisputed that a plan confers discretionary authority to determine eligibility and to interpret the plan, if an eligibility determination turns on a question of law, the reviewing court must apply a *de novo*

standard of review. Weil v. Retirement Plan Administrative Committee of the Terson Co., 913 F.2d 1045 (2d Cir. 1990), vacated in part on rehearing, 933 F.2d 106 (2nd Cir. 1991).

(d) Under Firestone, if a plan provides the plan administrator with discretionary authority to determine eligibility for benefits and to construe the terms of the plan, decisions of the plan administrator will be reviewed under the arbitrary and capricious standard rather than the *de novo* standard.

(i) Some courts have interpreted the arbitrary and capricious standard to require an evaluation of the reasonableness of a fiduciary's determination. In Lister v. Stark, 942 F.2d 1183 (7th Cir. 1991), the Seventh Circuit held that a fiduciary's interpretation of the plan should be given deference unless it is unreasonable. The court stated that a plan administrator's decision will be considered unreasonable where the fiduciary fails to consider important aspects of the issues involved, offers an explanation for its decision that runs counter to the evidence, or where the decision is so implausible that it cannot be ascribed to a difference in view or the product of the fiduciary's expertise.

(ii) Other courts have rejected the arbitrary and capricious standard in favor of an abuse of discretion standard. While most courts use the terms "arbitrary and capricious" and "abuse of discretion" interchangeably, the court in Nunez v. Louisiana Benefit Committee, 757 F. Supp. 726 (E.D. La. 1991), rejected the arbitrary and capricious standard in favor of an abuse of discretion standard stating that the court in Firestone explicitly rejected the arbitrary and capricious standard which would require the affirmation of a plan administrator's decision if any evidence existed to support it.

(iii) In Yusuf v. Yusov, 920 F.2d 937 (9th Cir. 1990), the Ninth Circuit held that under the arbitrary and capricious standard a court may reverse a denial of benefits only where a decision is made in bad faith, is not supported by substantial evidence, or is erroneous on a question of law.

(e) According to Firestone, the existence of a conflict of interest on the part of a plan fiduciary is relevant to the determination of whether the fiduciary's decisions will be entitled to deference.

(i) In Brown v. Blue Cross & Blue Shield of Alabama, Inc., 898 F.2d 1556 (11th Cir. 1990), *cert. denied*, 111 S.Ct. 712 (1991), the Eleventh Circuit held that "when a plan beneficiary demonstrates a substantial conflict of interest on the part of the fiduciary responsible for benefit determinations, the burden shifts to the fiduciary to prove that its interpretation of plan provisions was not tainted by self-interest." Id. at 1566. Brown involved an insured group health plan which was administered by the insurer providing coverage. The court held that an inherent conflict of interest existed between the roles assumed by the insurance company, since an insurance company pays claims out of its own assets rather than out of a trust, which places the insurance company's fiduciary role in conflict with its profit making role as a business. In such a situation, the court held that the fiduciary's determination will be arbitrary and capricious if it advances the fiduciary's self-interest at the expense of the beneficiary, unless the

fiduciary can justify its interpretation on the basis of the benefit provided to the entire class of plan participants.

(ii) In Callahan v. Rouge Steel Co., 941 F.2d 456 (6th Cir. 1991), in applying the arbitrary and capricious standard to a denial of severance benefits, the Sixth Circuit found that the fact that the employer was also the plan administrator created a conflict of interest and declined to hold as a matter of law that the employer/plan administrator did not act arbitrarily and capriciously in denying the benefits.

Note: Cases involving conflicts of interest on the part of plan administrators, although normally reviewable under an arbitrary and capricious standard, generally must survive a *de novo* standard of review in which the burden of proof will most likely be on the plan fiduciaries to justify their decision.

7. Other Issues

7.1 Employer Contributions

(a) Keystone Consolidated Industries, Inc. v. Commissioner, 951 F.2d 76, 14 E.B.C. 2284 (5th Cir. 1992), held that an employer's contributions of unencumbered property to satisfy its pension plan funding obligations were not prohibited transactions subject to excise taxes under the Internal Revenue Code (the "Code"). The employer contributed five truck terminals and real property to the trust to satisfy its minimum funding obligations. The terminals and property were not subject to mortgages and were not covered by employer lease-back agreements. The employer claimed deductions for the property's fair market value and reported the difference between its cost and fair market value at the time of the transfer as capital gains. The court held that §4974(f)(3) of the Code, which prohibits self-dealing transactions between an employer and a plan, states that a transfer of property encumbered by a mortgage or lien which a plan assumes shall be treated as a sale or exchange. The court concluded that this implies that the transfer of unencumbered property is not to be treated as a prohibited sale or exchange. The court further noted that §4971 of the Code, which imposes taxes on any funding deficiencies resulting from the contribution of overvalued assets, provides protection for potential abuse involving transfers of overvalued assets. The Supreme Court reversed the holding of the Fifth Circuit, ruling that because Congress intended §4975(f)(3) to expand, not limit, the scope of the prohibited-transaction provision to include contributions of encumbered property that do not satisfy funding obligations.

(b) Conversely, Wood v. Commissioner, 955 F.2d 908, 14 E.B.C. 2401 (4th Cir. 1992), held that an employer's transfer of promissory notes to satisfy his pension plan funding obligation was a prohibited transaction subject to excise tax under §4975(c) of the Code. The employer contributed three non-recourse promissory notes to the plan to meet its funding requirement. The notes were later paid in full and the employer claimed a deduction for the contribution in excess of the fair market value of the notes at the time they were transferred. The court held that §4975 of the Code involved a blanket prohibition on transactions between a plan and a disqualified person because of the inherent potential for abuse. The court stated that the purpose of the prohibition was to avoid contributions of overvalued property to the detriment of

the plan. The court noted that the DOL has interpreted a parallel provision in ERISA to bar the transfer of non-cash property to satisfy a plan sponsor's funding obligation.

7.2 §502(c)(1) Litigation

ERISA requires plan administrators to provide each participant with a summary plan description (ERISA §102; 29 USC §1022), a summary annual report (ERISA §104(b)(3); 29 USC §1024(b)(3)), and upon written request, a statement indicating the participant's total accrued benefits and his or her nonforfeitable interest (ERISA §105(a); 29 USC §1025(a)). §502(c)(1) of ERISA (29 USC §1132(c)(1)) requires plan administrators to comply with requests for information within 30 days.

(a) The courts are generally reluctant to impose liability under §502(c)(1) of ERISA for failure to comply with the reporting and disclosure requirements, holding that a participant will not be entitled to recover under §502(c)(1) unless the participant files a written request for information with the plan administrator. In Williams v. Caterpillar Inc., 944 F.2d 658 (9th Cir. 1991), the court held that a mere allegation that a plan administrator failed to provide a requested summary plan description ("SPD") will not establish a claim under §502(c)(1) of ERISA where the participant fails to offer proof that the SPD was ever requested from the plan administrator.

(b) Additionally, courts typically will deny recovery under §502(c)(1) of ERISA unless the participant can demonstrate that they have been prejudiced or harmed by the plan administrator's delay in providing the requested information, or that the plan administrator has acted in bad faith or intentionally failed to provide the information requested. In United Paperworkers International Union, Local 14 v. International Paper Co., 777 F. Supp. 1010 (D. Me. 1991), the court held that a participant did not have standing to complain of a plan administrator's violation of the reporting and disclosure requirements of ERISA absent a showing of some significant reliance on, or possible prejudice flowing from, the reporting and disclosure violations.

(c) In Starr v. JCI Data Processing, Inc., 767 F. Supp. 633 (D.N.J. 1991), the court imposed liability on an employer under §502(c)(1) of ERISA for failure to comply with the funding, participation, and vesting requirements of ERISA as well as the requirement that a plan be established and maintained pursuant to a written instrument. The employer acknowledged that the participant had requested general as well as specific information concerning the plan and his benefits, but declined to respond to the request because the plan administrator believed the participant knew he was not entitled to benefits under the plan, because the employer had no SPD, and because the plan administrator did not believe that the plan was subject to ERISA. The court did not require the participant to demonstrate specific harm resulting from the employer's failure to respond to his request, holding that the employer exhibited a lack of good faith in ignoring the participant's request.

(d) In Veilleux v. Atochen North America, Inc., 929 F.2d 74 (2nd Cir. 1991), the Second Circuit stated that in situations where violations of the ERISA disclosure provisions work a "substantive harm" on participants who are denied benefits, courts may find that the

violations warrant a finding that the denial of benefits was "arbitrary and capricious." In the situation presented, the court rejected the participants' claims due to the fact that they were unable to demonstrate any harm or prejudice resulting from the employer's failure to disclose the requested information.

However, the issue addressed by the Second Circuit of whether violations of reporting and disclosure requirements may give rise to liability for benefits under an ERISA plan is significant in that, unlike the damages that may be imposed under §502(c)(1) of ERISA, a finding that the denial of benefits under a plan is arbitrary and capricious directly impacts on the administration of the plan.

(e) Lee v. Benefit Plans Administration of Armco, Inc., S.D. Tex., No. H-90-3642 (4/30/92), found a pension plan administrator subject to ERISA's maximum \$100.00 per day penalty for failure to timely provide a participant with plan information. The court awarded the participant a total of \$7,800 in penalties against the administrator and \$25,000 for attorney's fee incurred at trial as well as \$5,000 in attorney's fees for a successful appeal to the Court of Appeals and an additional \$5,000 in attorney's fees for a successful appeal to the U.S. Supreme Court, should such appeals occur. The court held that the failure to provide timely information under ERISA, whether negligent or intentional, renders an administrator liable unless the failure results from a matter beyond the administrator's reasonable control. The court found that the administrator acted with deliberate indifference to its ERISA duties by failing to train its staff how to process requests for information or to advise the staff of the requirement that information be disclosed within 30 days.

7.3 Punitive Damages

It has generally been held that ERISA does not provide for the recovery of extra-contractual damages. According to §409(a) of ERISA (29 USC §1109), which establishes liability for breach of fiduciary duties, any fiduciary who is liable for a breach of fiduciary duty will be required to make good to the plan losses resulting from the breach, to restore to the plan any profits which the fiduciary received due to the improper use of plan assets and "shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary." §502(a) of ERISA (29 USC §1132(a)), which provides for civil enforcement procedures under ERISA, states that an action may be brought under §409 for breach of fiduciary duty by the Secretary of Labor, a participant, beneficiary or plan fiduciary for appropriate relief under §409 or for "other appropriate equitable relief." The courts have generally held that neither §409(a) or 502(a) of ERISA permits the recovery of extra-contractual or punitive damages.

(a) The Supreme Court in Massachusetts Mutual Life Ins. Co. v. Russell, 105 S.Ct. 3085 (1985), held that §409(a) of ERISA does not provide a cause of action for extra-contractual damages by a plan participant or beneficiary. The Court held that while §502(a)(2) of ERISA authorizes participants or beneficiaries to bring actions against a fiduciary for violation of §409 of ERISA, recovery for such violations inures to the benefit of the plan as a whole and not to the individual participant or beneficiary. The Court stated that the legislative history of ERISA indicated that the primary concerns in drafting §409 of ERISA were the possible misuse of plan assets and remedies that would protect the entire plan rather than the rights of an individual

beneficiary. Additionally, the Court noted that the statutory provisions under §502(a) of ERISA are silent as to the recovery of extra-contractual damages. The Court concluded that in enacting a comprehensive legislative scheme such as ERISA, which includes an integrated system of procedures for enforcement, Congress deliberately omitted any such remedy. The Court declined to address the issue whether §409 of ERISA authorizes the recovery of extra-contractual compensatory or punitive damages in an action by a plan against a fiduciary.

(b) In Drinkwater v. Metropolitan Life Ins. Co., 846 F.2d 821 (1st Cir. 1988), the First Circuit noted that while the Supreme Court's decision in Russell was limited to remedies available under §502 for violations of §409 of ERISA, the Court expressly reserved the question of whether extra-contractual damages might be a form of "other appropriate equitable relief" available under §502. However, the First Circuit agreed with and followed the holdings of other circuits that extra-contractual damages are unavailable under §502, and that the term "equitable" is meant to intend injunctive or declaratory relief.

(c) Diduck v. Kaszycki & Sons Contractors, Inc., 737 F. Supp. 792 (S.D.N.Y. 1990), held that punitive damages could not be sought under §409 of ERISA. The court stated that the §409(a) grant of authority permitting a court to award equitable relief does not encompass extra-contractual or punitive damages. In reaching its decision the court looked to the analysis of the circuits in determining whether §502(a) of ERISA encompasses extra-contractual or punitive damages for fiduciary violations. The court concluded that Congress intended for ERISA to incorporate the fiduciary principals of the law of trust, under which trustees are generally not liable for punitive damages for breach of fiduciary duty. Additionally, the court stated that ERISA's legislative history with regard to remedies for breaches of fiduciary duty contemplates traditional forms of equitable relief such as injunctions, constructive trusts, and the removal of fiduciaries.

(d) Although the Seventh Circuit in a previous decision left open the possibility of extra-contractual recovery under §502 of ERISA, the court held that such damages were not available where the only extra-contractual damages sought by the plaintiff were punitive in nature and the allegations in the complaint did not support a claim for such damages. The court, relying on the Supreme Court's holding in Firestone, *supra*, that ERISA is to be construed consistently with the common law of trusts, denied punitive damages as such damages are generally unavailable in the trust context. Petrilli v. Drechsel, 910 F.2d 1441 (7th Cir. 1990).

(e) In Gaskell v. Harvard Cooperative Society, 762 F. Supp. 1539, 14 EBC 1290 (D. Mass. 1991), the plaintiff, relying on the Supreme Court's decision in Ingersoll - Rand Co. v. McClendon, 111 S.Ct. 478 (1990), in which Justice O'Connor, in dicta, suggested that compensatory and punitive damages were within the power of federal courts to provide, sought such damages in relation to an ERISA violation by his employer. However, the court held that if the Supreme Court had intended to expand the realm of potential relief available under ERISA and to overrule its prior holdings, it would have done so explicitly and not in dicta. The court refused to overrule the express holding of the First Circuit in Drinkwater, *supra*, without a clear indication that the law will provide for extra-contractual damages under ERISA.

(f) In Novak v. Anderson Corp., 962 F.2d 757, 15 EBC 1127 (8th Cir. 1992). The court found that an ESOP participant was not entitled to monetary damages due to the employer's failure to notify the participant that his plan distribution could be rolled over into a tax deferred plan. The court held that the reference in §502(a)(3)(B) of ERISA to "other equitable relief" does not include monetary damages. The court concluded that neither the statutory language or the legislative history permits an expansion of the traditional equitable relief available - injunctive and declaratory relief and the imposition of a constructive trust - to include monetary damages.

7.4 SPD v. Plan Document

While many courts follow the language of the plan document rather than the terms of the summary plan description ("SPD"), courts are increasing likely to hold employers to the terms of the SPD where the terms of the SPD and the plan document are in conflict.

(a) In Heidgerd v. Olin Corp., 906 F.2d 903 (2nd Cir. 1990), the court held that where the terms of a plan and the SPD are in conflict the SPD will control. According to the court, the SPD should govern because, unlike the plan, it must be filed with the Secretary of Labor and distributed to employees. The court concluded that ERISA contemplates that the SPD should be the primary source of information upon which employees are entitled to rely and that to permit the plan to contain different terms that supersede the terms of the SPD would defeat the purpose of providing employees with such summaries.

(b) In Lasseter v. Administrative Committee of the Kieser Aluminum Salaried Employees Retirement Plan, 1991 U.S App. LEXIS 6202 (9th Cir. 1991), the Ninth Circuit denied participant benefits based on the language in the SPD. The SPD stated that an employee whose age and years of service totaled 70 or more could retire early with full benefits under the early retirement provisions upon the sale of the company. The plan was later amended to provide that the early retirement benefit was not available to any participant offered a suitable position by a purchaser of a division of the company. No new SPD was distributed to employees. However, the court concluded that the SPD added caveats to the eligibility criteria for early retirement which could not lead a reasonable person to believe that if his part of the company was sold, but operations continued and his job continued, that he could nevertheless elect early retirement.

(c) In Spivey v. Lincoln National Life Ins. Co., 1991 U.S. App. LEXIS 4439 (9th Cir. 1991), the court held that the plaintiff was not entitled to additional insurance proceeds upon the death of his participant spouse due to the fact that the deceased participant had never spent an "active day at work" in the position to which she was promoted prior to her death. The plaintiff husband alleged that the terms of the SPD were ambiguous and contradictory with regard to the term "active day at work." The court noted that the SPD explicitly stated: "If you are not actively at work on the date the amount of your insurance will otherwise be increased, such increase is not effective until the next following day on which you are actually at work." The court refused to require SPDs to contain specific information about all of the circumstances which could result in a loss of benefits so long as the SPD contained sufficient information to appraise participants that "danger lurked."

7.5 Plan Qualification and Disqualification

(a) In Lima Surgical Associates, Inc. VEBA v. U.S., 944 F.2d 885, 14 EBC 1346 (Fed. Cir. 1991), the court held that a purported VEBA did not qualify as a tax exempt VEBA because it provided benefits similar to pension or retirement benefits. The plan had filed an application for recognition of tax exempt status as a VEBA under §501(c)(9) of the Code which was denied by the IRS. After paying the income taxes assessed against the plan by the IRS the plan sought a refund. The court affirmed the decision of the Court of Claims denying the VEBA tax exempt status holding that although the plan provided for medical, life and accident benefits, it also provided for retirement benefits which do not qualify as "other benefits" under the VEBA rules.

(b) The court in Basch Eng'g, Inc. v. Comm'r, 59 T.C.M. (CCH) 482 (1990), permitted the retroactive revocation of a plan's qualified status due to the employer's failure to amend the plan on a timely basis to comply with changes in the tax law. The employer received a final adverse determination letter from the IRS indicating that the plan had not met the requirements for qualified status for years ending on or after March 31, 1985 due to the failure to amend the plan to comply with the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), the Tax Reform Act of 1984 ("TRA 84") and the Retirement Equity Act of 1984 ("REA"). The employer contended that the plan "substantially complied" with the requirements of TEFRA, TRA 84 and REA, and that none of the changes in those Acts would have any impact upon the operation of the plan. The court held the fact that the defective provisions in the plan were not operative did not mean that the plan satisfied the statutory requirements for qualification. The court concluded that the IRS, under the broad discretion granted it in §7805(b) of the Code, did not abuse its discretion in revoking the ruling retroactively.

(c) In TCS Manufacturing, Inc., Employee's Pension Trust v. Comm'r, 60 T.C.M. (CCH) 1312 (1990), the tax court held that a plan was disqualified due to the employer's refusal to amend the plan to meet certain conditions imposed on the qualification by the IRS in order for the plan to receive a favorable determination. The employer had adopted its pension plan prior to the enactment of ERISA and failed to amend the plan to comply with ERISA for a number of years. The employer received a retroactive favorable determination letter from the IRS which was conditioned upon eliminating excess contributions and including earnings allocable to the contributions in income. The court held that since the favorable determination letter was conditioned upon the employer meeting the contributions and earnings provisions, neither the plan nor the trust was qualified during the years in issue.



LITIGATION UNDER ERISA

Claimant Perspective

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SECTION H(b)



ERISA LITIGATION

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ERISA LITIGATION
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I. Introduction

This outline presents a summary view of litigation under the Employees Retirement Income Security Act ("ERISA), from the point of view of the plaintiff's counsel. It examines some of the issues that counsel should recognize and review when assessing potential ERISA claims and/or representing plaintiffs in ERISA and benefits cases. The author wishes to thank David M. Cook, David M. Cook, LLC, 22 West Ninth Street, Cincinnati, Ohio 45202, (513) 721-7500, for his assistance in this outline.

II. ERISA Preemption

ERISA (29 U.S.C. § 1000 et seq.) preempts and "supercedes any and all State laws insofar as they may now or hereafter relate to any employee benefit plan" as "employee benefit plan" is defined under ERISA. 29 U.S.C. § 11__ (a). A state law that "regulates insurance, banking, or securities" is not preempted, 29 U.S.C. § 11__(b)(2)(A), but that limitation is narrow. A state's "notice-prejudice" rule, for example, is not preempted, Unum Life Insur. Co. v. Ward, 526 U.S. 358 (1999), but a state law claim for "bad faith" on by an insurer is preempted. Massachusetts Cas. Ins. Co. v. Ryenolds, 113 F.3d 1450 (6th Cir. 1997). Thus, while state courts have concurrent jurisdiction over benefits claims as described below, those cases are removable; as a practical matter, all ERISA litigation is in federal court.

III. Types of Cases

A. A "participant" or "beneficiary" of an employee benefit plan may bring a civil action under 29 U.S.C. § 1132(a)(1)(B) "to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan." These benefits claims comprise the vast majority of ERISA cases brought in Kentucky.

B. A participant or beneficiary may bring a claim for breach of fiduciary duty under 29 U.S.C. § 1132(a)(2) "for appropriate relief under [ERISA] section 409," 29 U.S.C. § 1109. In

these claims, however, the plaintiff brings the claim on behalf of the plan, and the remedy must be paid to the plan. These cases can arise where a plan trustee or fiduciary mismanages the assets of a benefit plan such as a pension plan or 401(k) plan, or overpays for employer stock held by an employee stock ownership plan (“ESOP”), or really in any variety of ways. The requirement that the action be brought on behalf of the plan gives such actions many of the characteristics of a class or derivative action, although they are not technically Rule 23 class actions.

C. A plaintiff may bring a claim under 29 U.S.C. § 1132(a)(3)(B) “to obtain other appropriate equitable relief.” Claims brought under this section include claims brought by plan participants who believe that they were misinformed by their employers or plan fiduciaries a about their employee benefit. Varity Corp. v. Howe, 516 U.S. 489, 116 S.Ct. 1065 (1996); Krohn v. Huron Memorial Hospital, 173 F.3d 542 (6th Cir. 1999) (Hospital liable as fiduciary to respond to plaintiff-beneficiary's husband's request for benefits, and to alert LTD insurer that plaintiff had made an application for benefits). The Supreme Court has decided the issue of whether a health maintenance organization may be liable for breach of fiduciary duty under ERISA for refusing treatment. In Herdrich v. Pegram, 530 U.S. 211 (2000), the Court ruled that even though the defendant physicians managed the plan, including the doctor referral process, the nature and duration of treatment and every aspect of the HMO’s governance, and resolved disputed claims, they did not rise to the level of plan fiduciaries, because Congress intended for HMOs to operate in that manner. Trustees of plans also have standing to bring suit under this section. Harris Trust v. Salomon-Smith Barney, Inc., 530 U.S. 238 (2000).

D. Under 29 U.S.C. § 1140, it is unlawful “to discharge, fine, suspend, expel, discipline, or discriminate against a participant or beneficiary for exercising any right to which he is entitled under the provisions of an employee benefit plan” or ERISA, or “for the purpose of interfering with the attainment of any right to which such participant may become entitled.” This section was enacted primarily to prevent an employer from terminating employees just as their pensions were to vest, but it has been interpreted to prohibit an employer from interfering with an employee’s right to attain any other covered benefit.

E. While other causes of action exist, the other of note is one that arises under 29 U.S.C. § 1132(a)(1)(A) and (c), when an employer or a plan fails to provide participants with copies of plan documents that other sections of ERISA require to be provided to participants. The remedy for such failure can be up to \$110/day; a letter from the plaintiff’s attorney citing these sections will ordinarily convince the employer or plan to comply with its disclosure requirement. *See* Davis v. Featherstone, 97 F.3d 734 (6th Cir. 1996); Bartling v. Fruehauf Corp., 29 F.3d 1062 (6th Cir. 1994) (district court did not abuse discretion by considering defendant's good faith and lack of prejudice in not imposing penalty).

IV. Benefits Claims.

A. Benefits claims generally are those for short- or long-term disability benefits, for

payment or reimbursement of medical expenses under a health insurance plan, for severance pay under a severance pay plan, for retirement benefits (including disability retirement benefits), for group life insurance benefits, and for similar benefits. **Practice tip:** Group life insurance plans often contain disability clauses that provide continued insurance if the claimant becomes disabled, without further payment of premiums; this benefit is often forgotten, and it can be lost if not pursued promptly.

B. Claims procedures. ERISA requires that employee benefit plans have “reasonable” internal procedures under which a plan participant can make a claims for benefits. 29 U.S.C. § 1333. Ordinarily, a claimant must exhaust these procedures before filing a civil action. Ravencraft v. UNUM Life Ins. Co., 212 F.3d 341 (6th Cir. 2000). Typically, a claimant must make an initial claim for benefits, and the plan must respond within periods set forth in the regulation, depending on the type of claim. If the plan denies the claim, then the plan must explain the reasons for the denial in detail. The applicable regulation, 29 CFR 2560.503-1 (as amended, effective January 1, 2002 for non-health plans; health plans must establish new procedures by January 1, 2003), sets forth in detail what the claims procedures must include and how the plan must communicate with the claimant.

If the claim is denied, the claimant must then effectively appeal the decision (or make a “request for review” of the denial) to the plan administrator or other fiduciary, who (at least in theory) makes a “full and fair” review of the denial. Again, 29 CFR 2560.503-1 is the controlling regulation. The claimant may present additional evidence to support his claim and otherwise argue that he is entitled to the benefit in question. The plan administrator or fiduciary must then make a written ruling on the claim under the standards set forth at 29 CFR 2560.503-1(j). If the claim is denied, the writing must explain the specific reasons for the denial, set forth the claimant’s right to copies of all documents that the administrator used in denying the claim, and set forth the claimant’s appeal rights, including the right to file a civil action.

Practice tip: ERISA requires plans to prepare a “summary plan description” or SPD and provide a copy to participants. The SPD is supposed to be a plain-language description of the plan’s benefits and claims procedures. Try to get a copy of the SPD from your client or from the employer as soon in the process as possible. If the SPD differs from the actual plan document (which could be an insurance policy), then the SPD controls. University Hospitals of Cleveland v Emerson Electric Co., 202 F.3d 839, 851 (6th Cir. 2000).

Practice tip: 29 CFR 2560-503-1(h)(2)(iii) and (i)(5) requires the plan administrator to provide free copies of all materials used in denying the claim. Always request this material in writing as soon as the denial is received, because it is the bulk of the “administrative record” that the federal court will eventually review. Insurance companies and other plan administrators often try to slip additional material into the court record, and an early request for ALL material used in the administrative process will make this practice much more difficult.

Practice tip: When reviewing the plan administrator’s written denial, pay careful attention to

who actually made the decision to deny the benefit. Often, a plan document will designate a committee or other entity and ascribe to that committee the discretionary authority to make benefits decisions, but the actual decision to deny a benefit will have been made by the employer itself. When that occurs, the courts will NOT apply the arbitrary and capricious standard, because the decision was not “made in compliance with plan procedures.” Sanford v. Harvard Industries, Inc., 262 F.3d 590, 597 (6th Cir. 2001).

C. No Right To A Jury Trial. ERISA does not expressly provide for trial by jury for any causes of action it creates. Courts are now unanimous in holding benefit claims as well as claims for breaches of fiduciary duty and other statutory violations are equitable in nature and no right to a jury trial exists for such claims. See Adams v. Cyprus Amax Minerals Co., 149 F.3d 1156 (10th Cir. 1998) (no right to jury trial in §502(a)(1)(B) claims); Tischmann v. ITT/Sheraton Corp., 145 F.3d 561 (2nd Cir.), cert. denied, 119 S.Ct. 406 (1998); DeFelice v. American Intl. Life Assurance, 112 F.3d 61 (2^d Cir. 1997); Bittinger v. Tecumseh Products Co., 123 F.3d 877 (6th Cir. 1997). Instead, the district court’s job is limited to reviewing the decision of the plan administrator to deny the claim.

D. Standard of Review. The standard of review that the district court applies is **the key issue** in a case involving a claim for benefits.

1. The Firestone case. The seminal case on standard of review is Firestone Tire and Rubber Co. v. Bruch, 489 U.S. 101, 109 S.Ct. 948 (1989), in which the Court explained that principles of trust law supply the appropriate standard of review in ERISA benefits cases. The Court ruled that a district court is to review the administrator’s decision *de novo*, “**unless the benefit plan gives the administrator or fiduciary discretionary authority to determine eligibility for benefits or to construe the terms of the plan.**” *Id.*, at 115. When the plan does have such language, then the court reviews the decision under the “arbitrary and capricious” standard. Under the “arbitrary and capricious” standard, the issue for the federal court is not (for example) whether the plaintiff is actually disabled given the administrative record before it, but instead whether the plan administrator (often an insurance company) acted arbitrarily in denying the benefit.

“Under the deferential ‘arbitrary and capricious’ standard, courts will uphold a benefit determination if it is rational in light of the plan’s provision. Stated differently, when it is possible to offer a reason explanation, based on the evidence, for a particular outcome, that outcome is not arbitrary or capricious.” University Hospitals of Cleveland v. Emerson Electric Co., 202 F.3d 839, 846 (6th Cir. 2000)(internal quotations and citations omitted).

Naturally, after Firestone, benefit plans scurried to insert language that granted the plan administrator such discretionary authority. The practical effect of the ruling,

particularly when an insurance company is the plan administrator, is that the insurance company abandons its fiduciary duty to review the claim on its merits, and instead reviews the claim with the idea of showing to the federal judge that its denial of benefits was “rational in light of the plan’s provisions.”

2. Sixth Circuit Standard of Review Cases. The Sixth Circuit has issued several opinions under Firestone, and the earlier decisions were harsh on plaintiffs. See Yeager v. Reliance Standard Life Ins. Co., 88 F.3d 376 (6th Cir. 1996)(plan language requiring that a claimant submit “satisfactory proof of total disability to us” was sufficient to confer arbitrary and capricious review); Peruzzi v. Summa Medical Plan, 137 F.3d 431, 433 (6th Cir. 1997)(ruling that the inherent conflict of interest in a self-funded plan did not alter the standard of review, but “should be taken into account as a factor in determining whether the . . . decision was arbitrary and capricious”; the decision failed to indicate *how* the plaintiff could show the influence of the conflict); Borda v. Hardy, Lewis, Pollard Page, P.C., 138 F.3d 1062, 1066 (6th Cir. 1998)(under the arbitrary and capricious standard, the plan’s decision must be upheld if the decision was “rational in light of the plan’s provisions”).

The Sixth Circuit in recent decisions, however, has been more sympathetic to plaintiffs. In Sanford v. Harvard Industries, Inc., 262 F.3d 590, 597 (6th Cir. 2001), the court ruled that *de novo* review was appropriate because the *company* had made the decision to deny the benefit, and not the *plan trustee*, to whom the plan document had assigned authority to decide the claim. See also Williams v. International Paper Co., 227 F.3d 706 (6th Cir. 2000)(finding a plan interpretation to be arbitrary and capricious, regardless of the plan’s practice of consistently making the same interpretation on similar claims); Shelby County Health Care Corp. v. Southern Council of Workers Health & Welfare Trust Fund, 203 F.3d 926 (6th Cir. 2000)(finding a claims denial to be arbitrary and capricious where the plan’s interpretation of ambiguous provisions was not reasonable); University Hospitals of Cleveland v. Emerson Electric Co., 202 F.3d 839, 849 (6th Cir. 2000)(ruling that a plan’s interpretation of its pre-existing condition exclusion was contrary to plan language, and finding that the plan had “exceeded its power to *interpret* the Plan, and has instead effectively *rewritten* it”). University Hospitals also applied the “rule of *contra proferentum*” and construed ambiguities in the plan against the drafter of the plan. *Id.*, at 847. Finally, the case discussed conflicts of interests in note 4:

[W]e believe it appropriate to observe here that the mere existence of fiduciary duties, which always are present in any benefit determination governed by ERISA, does not obviate the need to more carefully examine decisions that might be tainted by a conflict of interest. Courts should be particularly vigilant in situations where, as here, the plan sponsor bears all or most of the

risk of paying claims, and also appoints the body designated as the final arbiter of such claims. Under these circumstances, the potential for self-interested decision-making is evident.

3. De Novo Review. In Wilkins v. Baptist Healthcare Sys., Inc., 150 F.3d 609 (6th Cir. 1998), the court made a variety of rulings that affect how ERISA claims are presented. First, it applied *de novo* review and upheld a denial of disability benefits. It also held that in the absence of a “due process” challenge to the claims process, a district court may not look at affidavits never reviewed by the plan administrator. The court also rejected a bench trial and the summary judgment process as the appropriate way to resolve ERISA benefit cases under a *de novo*. In such cases, evidence is limited to that considered by the plan (what is known as the “administrative record”), and a bench trial under Rule 52 or the summary judgment process under Rule 56 would be inappropriate.

E. Discovery. Generally speaking, there is no discovery in benefits cases, although courts may be willing to allow limited discovery on the actual contents of the administrative record, or how the inherent conflict of interest in a self-funded or insurance-based plan actually affected the plan’s determination. See Firestone Tire and Rubber Co. v. Bruch, 489 U.S. 101, 115, 109 S.Ct. 948 (1989)(“Of course, if a benefit plan gives discretion to an administrator or fiduciary who is operating under a conflict of interest, that conflict must be weighed as a ‘facto[r] in determining whether there is an abuse of discretion.’ Restatement (Second) of Trusts § 187, Comment *d* (1959)”).

F. The Administrative Record. Generally, after filing the Rule 26 report to the court, the court will order the parties to agree on the administrative record of the facts and documents that were before the plan administrator when it made the decision. The order will usually require the parties to enter into factual stipulations and to agree on the documents that the plan used to make its determination. Under 29 CFR 2560-503-1(i)(5) and (j)(3) and (m)(8), the plan must provide copies—before suit is filed—of “all documents, records, and other information relevant to the claimant’s claim for benefits,” which includes information that “was relied on in making the benefit determination,” or was “submitted, considered, or generated in the course of making the benefit determination.”

The parties will then file briefs, and the court will then make a ruling based on the administrative record and the briefs. The court will not look at materials or documents not before the administrator when it made the adverse benefit determination. This rule generally applies regardless of the standard of review. See Wilkins v. Baptist Healthcare Sys., Inc., 150 F.3d 609 (6th Cir. 1998); Yeager v. Reliance Standard Life Ins. Co., 88 F.3d 376 (6th Cir. 1996)(under arbitrary and capricious standard, a district court can only consider facts “known to” the plan at the time the decision was made). **Practice tip:** The Yeager case states that the court can consider what is “known to” the plan when it made its decision. Plaintiff’s counsel should therefore

insist on stipulations that fairly present what was known to the plan committee but not necessarily committed to paper.

G. Avenues For Avoiding The Arbitrary and Capricious Standard. The arbitrary and capricious standard is clearly an uphill struggle for a plaintiff, unless of course the plan simply failed to follow its own rules or ignored the record altogether. The first task for plaintiff's counsel, then, is to avoid the standard from the outset. The author suggest resolving the following questions to avoid the deferential standard:

1. Does ERISA even apply? ERISA does not apply to ALL benefit plans. "Governmental plans" are exempt from ERISA under 29 U.S.C. § 1003(b)(1). A governmental plan (29 U.S.C. § 1002(32)) is one sponsored by a governmental entity, which in Kentucky could include state government, hospital districts, water boards, libraries, cities, and a host of other entities. Many SPDs for such plans will include language that would lead the participate to believe that the plan is an ERISA plan, when in fact it is not. (Church plans are also exempt.) If the plan is a governmental or church plan, the case can be heard in state court (subject to being removed on diversity of citizenship grounds), before a local jury, in which the case is styled Local Citizen v. Out-of-State Insurance Company.

2. Did the employee pay for the benefit? ERISA may not apply to certain insurance benefits that an employee pays for through a payroll deduction. A benefit plan covered by ERISA is any "plan, fund, or program which [is] established or maintained by an employer or by an employee organization." 29 U.S.C. § 1002(1). The regulation pertaining to this definition (29 CFR 2510.3-1(j), known as the "safe harbor" regulation) excludes:

a group or group-type insurance program offered by an insurer to employees or members of an employee organization, under which

(1) No contributions are made by an employer or employee organization;

(2) Participation in the program is completely voluntary for employees or members;

(3) The sole functions of the employer or employee organization with respect to the program are, without endorsing the program, to permit the insurer to publicize the program to employees or members, to collect premiums through payroll deductions or dues checkoffs and to remit them to the insurer; and

(4) The employer or employee organization receives no consideration in the form of cash or otherwise in connection with the program, other than reasonable compensation, excluding any profit, for administrative services actually rendered in connection with payroll deductions or dues checkoffs."

See Thompson v. American Home Assurance Co., 95 F.3d 429 (6th Cir. 1996); B-T Dissolution, Inc. v. Provident Life & Accident Ins. Co., 175 F.Supp.2d 978 (S.D. Ohio 2001).

Thus, long-term disability policies that are paid for by the employee often are not covered by ERISA, and employee can bring a claim under those policies in state court, and again before a local jury.

3. Did the plan follow its own procedures in denying the claim? Under 29 CFR 2560.503-1(l), a plan's failure to establish and follow reasonable claims procedures allows the claimant to file suit without fully exhausting the plan's procedures. Presumably, the court would look at the claims file *de novo*, because there is simply no administrative ruling to be deferred to. **Practice tip:** The plaintiff's attorney should be completely unforgiving of a benefit plan that is even the slightest bit late in responding to a claim. File the suit as soon as it is clear that the time limits in 29 CFR 2560.503-1(i) have passed.

4. Did the plan assist the claimant secure Social Security benefits? Some if not most long-term disability benefit plans have provisions that require or encourage the claimant to make a claim for Social Security disability benefits. Believe it or not, many insurers will pay for an attorney to help the claimant pursue the Social Security claim, then (once the SSDI claim has been won) turn around and find that the claimant is not disabled under the terms of the policy. That fact pattern was the subject of blistering pro-plaintiff decision in Ladd v. ITT Corp., 148 F.3d 753, 756 (7th Cir. 1998).

H. Remedies. The remedy in a benefits claims case is the payment of the benefit; nothing will be awarded for extra-contractual damages. Davis v. Kentucky Finance Co. Retirement Plan, 887 F.2d 689, 696-97 (6th Cir. 1989), *cert. denied*, 495 U.S. 905 (1990) (and cases collected therein).

I. Attorney's fees. Attorney's fees may be awarded to the prevailing party under 29 U.S.C. § 1132 (g). Note that an award of fees and costs is discretionary, not mandatory; a prevailing party is not automatically entitled to a fee award. See McElwaine v. U.S. West, Inc., 176 F.3d 1167 (9th Cir. 1999); Doe v. Travelers Insur. Co., 167 F.3d 53 (1st Cir. 1999); Florence Nightingale Nursing Service v. Blue Cross/Blue Shield, 41 F.3d 1476 (11th Cir.), *cert. denied*, 514 U.S. 1128 (1995); Schake v. Colt Industries Op. Corp., 960 F.2d 1187 (3^d Cir. 1991); Anthuis v. Colt Industries Op. Corp., 971 F.2d 999 (3^d Cir. 1992). Also, a fee award can be made to either party; there is no limitation that fee awards be made only to "prevailing parties", although awards to prevailing defendants are rare.

In exercising their discretion under 29 U.S.C. § 1132(g)(1), the courts tend to consider what has become known as the "5 Factor Test". The application and relative weight of each factor tends to

vary from jurisdiction to jurisdiction. The 5 factors are:

- * the relative bad faith or culpability of the opposing parties;
- * the ability of the opposing party to satisfy an award;
- * the deterrent value of an award with respect to the offending party and others similarly situated;
- * the extent to which the party seeking fees sought to benefit all plan participants or to resolve a significant legal issue regarding ERISA; and
- * the relative merits of the parties' respective positions.

Wells v. U.S. Steel & Carnegie Pension Fund, 76 F.3d 731 (6th Cir. 1996); Armistead v. Vernitron Corp., 944 F.2d 1287 (6th Cir. 1991). In the Sixth Circuit, fees are awarded only for work done in connection with the litigation of the claim, and not for work done in the administrative process. Anderson v. Procter & Gamble Co., 220 F.3d 449 (6th Cir.2000).

V. Breach of Fiduciary Duty Claims

A. There are two general types of claims for breach of fiduciary duty. The first, under 29 U.S.C. § 1132(a)(2), allows a participant to bring a claim on behalf of the benefit plan “for appropriate relief under [ERISA] section 409,” 29 U.S.C. § 1109. As noted above, however, the plaintiff brings the claim on behalf of the plan, and the remedy must be paid to the plan. The second type of case may be brought by one or more plaintiffs under 29 U.S.C. § 1132(a)(3)(B) “to obtain other appropriate equitable relief.”

1. The claims under ERISA § 409 are made against a “fiduciary” of the plan, and typically raise issues that would have arisen under the common law of trusts. ERISA imposes a duty under 29 U.S.C. § 1104(a)(1) for the plan fiduciary to:

discharge his duties with respect to the plan solely in the interest of participants

and beneficiaries and—

(A) for the exclusive purpose of

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of the plan;

(B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;

- (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and
- (D) in accordance with the documents and instruments governing the plan insofar as such documents and instruments are consistent with the provisions of this title and title IV.

See, e.g., Chao v. Hall Holding Co., 285 F.3d 415 (6th Cir. 2002), and cases cited therein.

These cases arise in a lot of contexts, but primarily involve either a fiduciary's self-dealing or its failure to invest plan assets prudently. From the point of view of plaintiff's counsel, these cases usually involve substantial sums of money and affect a great number of persons. **Practice tip:** A transaction known as a "leveraged" employee stock ownership plan, where an ESOP is created and then caused to borrow money to purchase the stock of a retiring or departing company executive, is a particularly fertile ground for litigation, because the incentives for self-dealing typically overwhelm the parties involved. Chao v. Hall Holding Co., 285 F.3d 415 (6th Cir. 2002). This author believes, in fact, that it is virtually impossible to implement a leveraged ESOP transaction without somebody's breaching a fiduciary duty to the plan.

2. The claims under 29 U.S.C. § 1132(a)(3)(B) "to obtain other appropriate equitable relief" present a variety of fact patterns. *See* Varity Corp. v. Howe, 116 S.Ct. 1065 (1996)(parent corporation re-shuffled all its money-losing divisions (and their employees) into a new subsidiary, which became insolvent and unable to pay benefits promised employees when they transferred); Krohn v. Huron Memorial Hospital, 173 F.3d 542 (6th Cir. 1999) (Hospital liable as fiduciary to respond to plaintiff-beneficiary's husband's request for benefits, and to alert LTD insurer that plaintiff had made an application for benefits); Sprague v. General Motors Corp., 92 F.3d 1425 (6th Cir. 1996)(seeking to enforce promise of retiree medical benefits; these cases are very hard to win); McAuley v. International Business Machines Corp., 165 F.3d 1038 (6th Cir. 1999)(severance pay case arising out of IBM's offer of severance package in reduction-in-force; where an enhanced severance package is under "serious consideration," the employer or fiduciary is under a fiduciary obligation to inform the potential participants of the enhanced package).

B. Discovery. Discovery in breach of fiduciary duty actions is taken the same way as any other civil action in federal court.

C. Jury Trial. There is no right to a jury trial in breach of fiduciary duty cases. The remedy is considered to be equitable, and any trial will be to the bench.

D. Remedies. Remedies are equitable, not legal, and the plan is typically seeking its losses arising out of the defendant's conduct. Individuals are also able only to receive equitable relief, such as restitution. This has created a mass of confusing and often contradictory rulings on remedies, an explanation of which is beyond the scope of this outline. For an example, see Great-West Life & Annuity Ins. Co. v. Knudson, 122 S.Ct. 708 (2002). Counsel confronted with a breach of fiduciary duty case under 29 U.S.C. § 1132(a)(3)(B) "to obtain other appropriate equitable relief" should review relevant cases carefully when drafting the prayer for relief.

VI. Claims Under ERISA § 510, 29 U.S.C. § 1140

A. As noted above, ERISA § 510 is ERISA's anti-discrimination and anti-retaliation provision. The section makes it unlawful to discharge or discriminate against a person for exercising any right to which he is entitled under the provisions of an employee benefit plan or ERISA, or "for the purpose of interfering with the attainment of any right to which such participant may become entitled." The purpose of § 510 is to prevent an employer from taking actions such as discharging or discriminating against participants and beneficiaries for exercising their rights under a plan or under the statute. Lojek v. Thomas, 716 F.2d 675, 680 (9th Cir. 1983). Thus, § 510 prohibits an employer from taking actions "that might interfere with a person's ability to collect present or future benefits or which punish a participant for exercising his or her rights under an employee benefit plan." Tolle v. Carroll Touch, Inc., 977 F.2d 1129, 1139 (7th Cir. 1992); see also Majewski v. Automatic Data Processing, 274 F.3d 1106, 1113 (6th Cir. 2001)(finding ERISA §510 protects rights to *future* benefits as well as accrued benefits). It is now clear that § 510 applies to welfare benefit plans, which do not automatically vest, as well as pension plans. Inter-Modal Rail Employees Ass'n v. Atchison Topeka & Santa Fe Ry. Co., 520 U.S. 510 (1997).

B. Right to a Jury Trial. It is unclear whether a § 510 claim can be tried to a jury. While many cases have held to the contrary, there is some Sixth Circuit authority that would support a jury trial. Pennington v. Western Atlas, Inc., 202 F.3d 902 (6th Cir. 2000) (jury that decided an ADEA claim acted as an advisory jury on an ERISA § 510 claim); Walsh v. United Parcel Service, 201 F.3d 718 (6th Cir 2000) (indirectly suggesting jury right in a 510 action if a genuine issue of fact had existed about whether non-discriminatory reason for discharge was pretextual)

C. Statute of Limitations. ERISA § 510 does not contain a specific limitations period, but courts have applied state statute of limitations pertaining to claims of wrongful discharge or employment discrimination. When analyzing the statute of limitations, courts look at the requested relief such as back and front pay, reinstatement, benefits, and the type of claim, such as, retaliation or discharge. See, e.g., Burrey v. Pacific Gas & Elec. Co., 159 F.3d 388 (9th Cir. 1998) (one-year limitation period for wrongful termination against public policy applies to transfer to leasing company); Musick v. Goodyear Tire & Rubber Co., Inc., 81 F.3d 136, 139 (11th Cir. 1996) (refusing to apply state contract period; applying two-year limitations period

without deciding whether retaliatory discharge or wage law is most appropriate); Ellis v. Ford Motor Co., 92 F.3d 1185 (6th Cir. 1996) (table) (borrowing state employment discrimination limitations period);

D. Prima Facie Cases and Shifting Burdens. ERISA § 510 is handled much like discrimination cases, where the plaintiff must state a *prima facie* case, and the burden shifts from one party to the other. The Sixth Circuit set forth the analysis in Smith v. Ameritech, 129 F.3d 857, 865 (6th Cir. 1997):

To state a claim under § 510, the plaintiff must show that an employer had a specific intent to violate ERISA. In the absence of direct evidence of such discriminatory intent, the plaintiff can state a *prima facie* case by showing the existence of (1) prohibited employer conduct (2) taken for the purpose of interfering (3) with the attainment of any right to which the employee may become entitled. Although ... not classif[ied] ... as part of the plaintiff's *prima facie* case, ... a plaintiff must show a causal link between pension benefits and the adverse employment decision. In order to survive [the] defendants' motion for summary judgment, [the] plaintiff must come forward with evidence from which a reasonable jury could find that the defendants' desire to avoid pension liability was a determining factor in [the] plaintiff's discharge. . . . [I]n an interference claim, the alleged illegal activity will have a causal connection to the plaintiff's ability to receive an identifiable benefit. [Internal citations and quotations omitted.]

See also Pennington v. Western Atlas, Inc., 202 F.3d 902 (6th Cir. 2000); Humphreys v. Bellaire Corp., 966 F.2d 1037 (6th Cir. 1992) (holding that “the proximity to vesting provides at least some inference of intentional, prohibited activity” sufficient to survive a *prima facie* case.

E. Class Actions. ERISA § 510 can be applied to classes as well. See Millsap v. McDonnell Douglas Corporation, 162 F.Supp2d 1262 (N.D. Okla. 2001)(finding that McDonnell-Douglas closed a plant to avoid employee benefit obligations).

ARBITRATION OF EMPLOYMENT DISPUTES

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ARBITRATION OF EMPLOYMENT DISPUTES

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INTRODUCTION

On March 21, 2001, the U.S. Supreme Court held that victim-initiated employment claims -- including statutory employment claims -- can be subject to mandatory arbitration. *Circuit City Stores v. Adams*, 532 U.S. 105 (2001). The *Circuit City* case is perhaps one of the most significant employment decision in 25 years. It is not an overstatement to say that the decision could potentially abolish *victim-initiated*, employment-related lawsuits should all employers choose to implement mandatory arbitration agreements.¹

I. WHY THE CIRCUIT CITY CASE IS IMPORTANT FROM A PRACTICAL STANDPOINT

There are three major reasons the *Circuit City* decision is important: (i) it will allow employers to try cases in a friendlier forum -- in front of an arbitrator, as opposed to an often hostile jury capable of rendering a "runaway" verdict; (ii) it is unlikely that arbitration will result in the "jumbo" settlements that have become commonplace in employment lawsuits; and (iii) the arbitration process is generally more expedient and less expensive for employers. Each of these reasons is significant with respect to an employer's ability to defend against employment claims made by a current or former employee.

¹ It is important to emphasize that the *Circuit City* case only addresses employment-related lawsuits initiated by the victim. As will be demonstrated in a later section of this paper, an employment-related lawsuit initiated by the Equal Employment Opportunity Commission ("EEOC"), on behalf of a current or former employee, is not unlawful, despite the existence of a valid and enforceable arbitration agreement between the employer and employee. *Equal Employment Opportunity Commission v. Waffle House, Inc.*, 534 U.S. 279 (2002).

A. Employers Are Losing More Often And “Bigger” Than At Any Time In Recent Years.

A recent *USA Today* article reported that the probability of a plaintiff prevailing in an employment suit has gone from 49% in 1994 to 71% in 1999. Equally troubling is the average recovery in these types of cases. Again, according to *USA Today*, the median compensatory damages award received by plaintiffs in employment cases has gone from \$127,500 in 1996 to \$200,000 in 1999. More troubling are the recent cases in which juries have awarded plaintiffs small fortunes in employment suits:

1. In *Dawson v. Starkey Lab*, a plaintiff claimed that she was terminated without cause after she refused to sign an agreement giving up her right to deferred compensation. **A jury awarded her \$62,000,000;**
2. In *Sonnier v. Farmers Insurance Exchange*, a plaintiff claimed he was terminated because he objected to being asked to engage in bad faith claims practices. **A jury awarded him \$10,456,000;**
3. In *McCarthy v. The Ground Round*, plaintiffs claimed wrongful discharge and age discrimination after the defendant discharged them during a reorganization and hired new people in allegedly new positions. **The jury awarded them \$6,692,402;**
4. In *Hughes v. K-Mart*, the plaintiff claimed she was fired in retaliation for complaining about wage discrimination. **The jury awarded her \$6,218,700;**

5. In *Clifton v. Massachusetts Bay Transportation*, a plaintiff claimed that he was racially harassed in his position as foreman. There was name calling, he was shot at with bottle rockets and firecrackers, and his locker was defaced with racist epithets. **The jury awarded him \$5,500,000;** and
6. position as a computer consultant after returning from maternity leave. She was allegedly told that she was being terminated because she was a woman with a family. **The jury awarded her \$5,500,000.**

In addition, when plaintiffs prevail on statutory employment claims, most statutes also require the employer to pay the plaintiff's attorney fees -- which can frequently equal or exceed the cost of the judgment.

B. Employee Lawsuits Are Resulting In Huge Settlements.

Newspapers have been replete in recent years with record breaking settlements in employment lawsuits. The following are just a few well-publicized settlements:

1. On November 28, 2000, a group of black, hourly employees at Texaco received a \$140,000,000 settlement arising out of their claims of racial discrimination;
2. On December 13, 2000, temporary employees at Microsoft agreed to settle a class action for \$97,000,000;

3. On October 7, 2000, black employees at the Federal Deposit Insurance Corporation tentatively agreed to settle their claims of race discrimination for \$14,000,000;
4. On November 18, 2000, 14 women employed by Ford Motors were paid a \$9,000,000 settlement in a sexual harassment case; and
5. In June 1998, Mitsubishi made a \$34,000,000 settlement in a sexual harassment/discrimination case.

While the above settlements all involve classes or multiple plaintiffs, employers are paying more to settle individual claims as well. Many employers feel it more prudent to settle employment claims rather than risking an adverse jury verdict.

C. Employers Are Spending Significant Sums To Defend Employment Lawsuits.

With attorney rates exceeding \$250 an hour in most regions, the cost of defending employment suits has escalated. Moreover, with the "scorched-Earth" discovery tactics employed by both defense and plaintiff counsel, it is not unusual for fees to exceed \$100,000 even before trial. Fees through trial, post-trial motions and appeal can easily approach \$150,000 to \$200,000. In addition to attorney fees, an employer is also responsible for its deposition costs and expert witness fees. All of these costs and fees add up, especially when you consider that most cases take up to two years to even get to trial.

Against this backdrop, employers have been looking for alternatives to employment litigation. Arbitration is that alternative, and employers would be remiss

if they did not consider its application. At a minimum, employers should be familiar with the process and its potential benefits.

II. WHAT IS ARBITRATION AND WHY WOULD AN EMPLOYER BENEFIT FROM THE PROCEDURE?

Arbitration has been aptly defined as a “simple proceeding voluntarily chosen by parties who want a dispute determined by an impartial judge of their own mutual selection, whose decision, based on the merits of the case, they agree in advance to accept as final and binding.” Elkouri & Elkouri, *How Arbitration Works* at 2 (4th Ed. 1985), *quoting* Chappell, *Arbitrate ... And Avoid Stomach Ulcers*, 2 Arb. Mag. Nos. 11-12, pp. 6-7 (1944). While this quote speaks to the **mutual** advantages of arbitration, the procedure is often advocated by employers for a number of reasons:

1. Employers see arbitration as a way to avoid runaway jury verdicts. Many commentators attribute the increase in runaway verdicts to juries reacting emotionally to employee claims, as opposed to simply applying the law. An advantage to arbitration is that cases are generally heard by a single arbitrator who is presumably trained in employment law. It is less likely that an arbitrator will be swayed by pure emotion. Even where an arbitrator finds that an employee’s legal rights have been violated, it is anticipated that the arbitrator will

fashion a remedy commensurate to the harm, and not award a financial windfall;²

2. Requiring an employee to submit employment claims to arbitration should also help employers in settling such claims. If a plaintiff and his/her counsel know from the outset they do not have an opportunity to make an emotional plea to a jury, it is likely that they will not value their employment claims as highly as they would have in recent years. This, in turn, should help employers to better posture these cases for settlement; and
3. Arbitration can be more expedient and less costly than civil litigation. Claims can be heard in a matter of months, as opposed to years. Discovery procedures and depositions -- while available -- can be limited by an arbitrator.

Given the foregoing, it is easy to see why so many employers are encouraged by the Supreme Court's decision in *Circuit City*. Before implementing an arbitration procedure, however, it is necessary to understand the issues *Circuit City* addressed, as well as those it left unresolved.

² Because the use of arbitration in employment claims is still a recent phenomenon (and because most employment arbitration decisions are confidential), there is no real track record for predicting employer success. However, in labor arbitrations in the union setting, employers appeared to have won approximately 70% of all arbitrations held in 2000. Bureau of National Affairs (Labor Arbitration 2000).

III. AN OVERVIEW OF THE *CIRCUIT CITY* DECISION

Circuit City utilized an employment application which provided that “all ... claims, disputes or controversies arising out of or relating to my ... employment with Circuit City would be resolved exclusively by final and binding arbitration before a neutral arbitrator.” *Id.* slip op. at 2. The application specifically identified all claims arising under federal, state or local statutory or common law as well as the Age Discrimination in Employment Act (“ADEA”), Title VII of the Civil Rights Act of 1964 (“Title VII”) and the Americans with Disabilities Act (“ADA”), as being subject to this provision.

Saint Claire Adams applied for employment with Circuit City in October 1995, and was hired as a sales consultant in Circuit City’s Santa Rosa, California store. Two years later, he filed an employment discrimination lawsuit against Circuit City in state court, asserting claims under California’s Fair Employment and Housing Act. Circuit City responded by filing suit in the federal district court, seeking to enjoin the state court action and to compel arbitration of Adams’ claims, pursuant to the Federal Arbitration Act (“FAA”).

The federal district court held that Adams was obligated by the arbitration provision in his employment application to submit his claims to binding arbitration. Adams appealed this decision. While Adams’ appeal was pending, the Ninth Circuit Court of Appeals held in another case that the FAA did not apply to contracts of employment. In reaching this result, the Ninth Circuit relied on language in the FAA which excludes from its coverage “contracts of employment of seamen, railroad

employees, or any other class of workers engaged in foreign or interstate commerce....” The court then applied its ruling to Adams’ appeal and held that the language in Circuit City’s employment application constituted an employment contract which was not subject to arbitration.

The Supreme Court reversed and remanded the Ninth Circuit decision, holding instead that the FAA exempted from its coverage “only contracts of employment of transportation workers.” All other employment contracts may be subject to mandatory arbitration. The Court also pointed out that in requiring employees to submit their employment disputes to binding arbitration, employers are not depriving employees of their substantive statutory rights. They are merely committing the dispute to an arbitral, rather than judicial, forum.³

Finally, the Court commented on the deference -- if any -- that should be paid to state arbitration statutes, *i.e.*, laws that prohibit employers from utilizing mandatory arbitration agreements. Responding to criticism that its holding would preempt states’ power to limit the arbitrability of certain employment disputes, the Court reiterated its holding in *Southland Corp. v. Keating*, 465 U.S. 1 (1984), that the FAA applies in state courts and preempts contrary state anti-arbitration laws. Among

³ The plaintiff in *Circuit City* brought claims under California’s Fair Employment and Housing Act and other claims based on general tort theories. Federal courts have also enforced mandatory arbitration of a broad range of statutory claims, including the following: Title VII, *see, e.g., Cole v. Burns Int’l Security Servs.*, 105 F.3d 1465 (D.C. Cir. 1997); the ADA and Family and Medical Leave Act (“FMLA”), *see, e.g., Miller v. Public Storage Management, Inc.*, 121 F.3d 215 (5th Cir. 1997); *Savarin v. A.G. Edwards & Sons, Inc.*, 971 F.Supp. 609 (N.D. Tex. 1996); and the Employee Retirement Income Security Act (“ERISA”), *see, e.g., Pritzker v. Merrill Lynch*, 7 F.3d 1110 (3d Cir. 1993).

these provisions is KRS 336.700 -- Kentucky's anti-arbitration statute -- which prohibits an employer from requiring an employee or person seeking employment to arbitrate "any existing or future claim, right, or benefit to which the employee or person seeking employment would otherwise be entitled under any provision of the Kentucky Revised Statutes or any federal law" as a condition or pre-condition of employment. Many other states have similar statutes restricting arbitration. Under the Supreme Court's holding in *Southland Corp. v. Keating*, the FAA preempts any inconsistent state law.

IV. THE SUPREME COURT IN *CIRCUIT CITY* LEFT MANY ISSUES UNRESOLVED

Given the reaction to its decision, one might assume that the Supreme Court had issued the final word on employment arbitration. However, the Court did not place its imprimatur on the *Circuit City* arbitration program, the specifics of which were not even mentioned.⁴ Instead, the Court left for another day the difficult issues

⁴ In fact, on remand, the Ninth Circuit held that, under California law, Circuit City's arbitration program was unenforceable because it contained procedurally and substantively unconscionable provisions and such provisions could not be severed. *Circuit City Stores v. Adams*, 279 F.3d 889 (9th Cir. 2002). In addition, a number of other state and federal courts have held portions of the Circuit City program to be contrary to the public policies underlying various civil rights statutes. See, e.g., *Johnson v. Circuit City Stores, Inc.*, 203 F.3d 821, 2000 WL 19166 (4th Cir.) (unpublished), cert. denied, 530 U.S. 1276 (2000); *Gannon v. Circuit City Stores, Inc.*, 2001 WL 930550 (8th Cir. 8/17/2001) (provision in arbitration agreement limiting punitive damages held invalid, but it could be severed and remainder of agreement enforced); *Wright v. Circuit City Stores, Inc.*, 82 F.Supp. 2d 1279 (N.D. Ala. 2000) (holding that although provision limiting award of punitive damages and back/front pay precluded employee from meaningful opportunity to vindicate statutory rights, rule of severability applied to uphold the arbitration agreement with

concerning how a mandatory arbitration program should be structured, how (or even if) it should be reviewed by courts, and the balance between federal and state law which is inherent in the FAA. The Court also failed to address whether a valid arbitration agreement between an employer and employee would preclude employment litigation *initiated by a federal agency* on behalf of the employee.

The unresolved issues fall within one of three major categories: (a) state law issues concerning contract formation and enforcement; (b) federal issues relating to arbitration procedures, judicial review, the interaction/involvement of the National Labor Relations Board (“NLRB”), and the preclusive effect of arbitration awards; and (c) federal issues relating to the EEOC’s position regarding mandatory arbitration agreements and the lawfulness of an EEOC-initiated employment action, on behalf of a current or former, when there exists a valid and enforceable arbitration agreement between the employer and the employee.⁵

A. Contract Formation Issues

Arbitration is a “creature of contract.” What that means is that an employer and employee(s) must have an agreement to submit an employment dispute to arbitration. What constitutes an “agreement,” however, is an issue the Supreme Court did not address. To address the issue, you must first answer the following questions:

modification of remedies to provide the full range of remedies available by statute). *Compare, Morrison v. Circuit City Stores, Inc.*, 70 F.Supp. 2d 815 (S.D. Ohio 1999).

⁵ This question has actually now been resolved by the Supreme Court in *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002).

1. **What assent on the part of an employee is necessary to support an agreement to arbitrate?**

Although arbitral contract formation is a matter of state law, *see, Patterson v. Tenet Healthcare, Inc.*, 113 F.3d 832, 834 (8th Cir. 1997); *Geiger v. Ryan's Family Steak Houses, Inc.*, 134 F.Supp.2d 985 (S.D. Ind. 2001), in *Circuit City*, the Supreme Court implicitly endorsed a simple means to obtain such assent in the application process:

I agree that I will settle any and all previously unasserted claims, disputes or controversies arising out of or relating to my application or candidacy for employment, employment and/or cessation of employment with Circuit City, *exclusively* by final and binding *arbitration* before a neutral Arbitrator. By way of example only, such claims include claims under federal, state, and local statutory or common law, such as the Age Discrimination in Employment Act, Title VII of the Civil Rights Act of 1964, as amended, including the amendments of the Civil Rights Act of 1991, the Americans with Disabilities Act, the law of contract and the law of tort.

Circuit City, 2001 WL 273205, slip op. at p.2 (emphasis in original).

As with contracts in general, courts have not been receptive to challenges claiming that an employee did not read the agreement or understand its terms. *See, e.g., Flynn v. Aerchem, Inc.*, 102 F.Supp.2d 1055, 1060 (S.D. Ind. 2000) (rejecting employee's claim that she was forced to sign the agreement while under economic duress and without knowledge of its contents); *Walker v. MDM Services Corp.*, 997 F.Supp. 822 (W.D. Ky. 1998).

2. **Does an employee have to sign a written arbitration agreement?**

Some courts have found there is no need for a signed arbitration agreement between the parties. *See, e.g., Brown v. J.C. Penney Co.*, Civil Action No. 3:97-CV-499-R (W.D. Ky. 1/8/1998) (attached at Tab 1); *Jenkins v. Workman*, Empl. Prac. Cas. (BNA) 7612, 2000 WL 962821 (S.D. Ind. 2000) (upholding validity of arbitration program, noting the employee did not have to sign form for agreement to exist); *Nghiem v. NEC Elec., Inc.*, 25 F.3d 1437, 1439-40 (9th Cir.), *cert. denied*, 513 U.S. 1044 (1994) (arbitration program valid where employee received but did not sign handbook containing program); *Kinnebrew v. Gulf Ins. Co.*, 67 Fair Empl. Prac. Cas. (BNA) 189, 1994 WL 803508 (N.D. Tex. 1994) (court compelled arbitration where an employer mailed its employees copies of its arbitration policy without explaining its effect or seeking the employees' agreement to the policy; simply receiving a copy of the arbitration policy and continuing to be employed was sufficient to bind the employees to submit any employment claim to arbitration). *Compare Romo v. Y-3 Holdings, Inc.*, 105 Cal.Rptr.2d 208 (Cal. Ct. App. 2001) (California Court of Appeals panel held that an employee's signature acknowledging that she signed for, received, understood, and agreed to the terms in an employee handbook did **not** bind her to an arbitration agreement set forth in the handbook).

Although an employer generally need not have a signed agreement with its employees to enforce an arbitration clause, a signed agreement is the best evidence of an employee's assent to arbitrate employment claims. However, obtaining signed agreements is particularly troublesome in situations involving current employees. If

an employee refuses to sign, the employee would be forced to do one of two things. First, the employer could make signing a condition of continued employment. If the employee refused to sign, he/she could be terminated. Such a course probably presents the ideal scenario for the EEOC to seek an injunction on a theory that the employer was interfering with its employees' statutory rights under Title VII and related employment laws. Or, second, the employer could simply advise the employee of the implementation date for the arbitration procedure. Should the employee continue working after that date, the employer could argue that the employee had acquiesced to the arbitration procedure. Of course, the employer would likely incur the wrath of the employees who did sign. Moreover, employees who did not sign could argue that the employer's acquiescence to their not signing waives the employer's right to enforce the agreement.

3. Does a statute need to be specifically referenced in an arbitration clause?

An issue exists as to whether an arbitration clause must refer to a particular statute in order to be enforceable with respect to that statute. This will, again, require a review of state contract law. As noted in Kraus and Vuchlewski, *Alternative Dispute Resolution: Arbitration of Statutory Discrimination and Other Employment Claims*, American Bar Association, March 1998 ("*Alternative Dispute Resolution*"): "The fact that an arbitration clause does not make specific reference to a particular civil rights statute does not necessarily negate its enforceability. So long as the arbitration provision makes reference to disputes between the employee and

employer in a way that encompasses employment discrimination and/or wrongful termination, it will most probably withstand judicial scrutiny.” *Id.* at 5.

However, courts generally require that an employee knowingly and voluntarily waive statutory rights. Unless the specific statute is set forth in the arbitration agreement, an employee could certainly make an argument that he/she did not knowingly and voluntarily waive the right to pursue an action in state or federal court under that statute.

B. Is the Arbitration Agreement Enforceable?

A critical question to enforcing arbitration agreements relates to the issue of legal consideration, *i.e.*, what does an employee get in exchange for agreeing to submit his/her claim to arbitration? Depending upon the timing, consideration in these cases is usually deemed to be the offer of employment, or in the case of a current employee, the promise of continued employment.

1. When an employee is hired -- the offer of employment

The *Circuit City* decision at least implies that federal courts will endorse agreements accepted in the application process. State courts have likewise enforced agreements entered into at the beginning of employment. *See, e.g., Gibson v. Neighborhood Health Clinics, Inc.*, 121 F.3d 1126 (7th Cir. 1997) (applying Indiana law, initial offer of employment may constitute consideration for an employee’s promise to submit claims to arbitration); *Ryan’s Family Steakhouse, Inc. v. Brooks-Shades*, 781 So.2d 215 (Ala. 2000) (affirming trial court’s dismissal of employee’s claims based on signed arbitration agreement); *Mueller v. Hopkins & Howard, P.C.*,

5 S.W.3d 182 (E.D. Mo. 1999); *Armendariz v. Foundation Health Psychcare*, 99 Cal.Rptr.2d 745 (Cal. 2000); *Walker*, 997 F.Supp. 822 (S.D. Tex. 1997).

2. For current employees -- is continued employment sufficient consideration?

Whether continued employment is sufficient consideration to enforce an arbitration agreement depends on each state's laws regarding contract formation. As a general rule, however, most states have found that an employer's offer to continue a current employee's employment -- albeit on "at-will" terms -- is sufficient consideration to support an arbitration agreement. *Craig v. Brown & Root, Inc.*, 100 Cal.Rptr.2d 818 (Cal. Ct. App. 2000) (a party's acceptance of an arbitration agreement can be implied-in-fact where the employee's "continued employment constitutes her acceptance of an agreement proposed by her employer"); *Kreimer v. Delta Faucet Co.*, 2000 WL 962817 (S.D. Ind. 2000) (employee became bound by the arbitration agreement by receiving the benefit of continued employment for "more than a year after she signed the acknowledgment form"); *Patterson*, 113 F.3d 832 (an arbitration clause contained in an employee handbook, signed by the employee after four years of employment, was a valid and enforceable arbitration agreement); *Brown v. J.C. Penney Co.*, (W.D. Ky. 1/8/1998) (continued employment constitutes sufficient consideration to support a binding arbitration agreement, even where the employee did not sign an agreement). *Compare, Environmental Products Co. v. Duncan*, 285 S.E.2d 889 (W.Va. 1981) (continued employment is insufficient

consideration to support covenant not to compete after employment has been commenced without such a restriction).

3. Other forms of consideration

Courts have also recognized forms of consideration other than continued employment. In *Flynn*, the court found that consideration was evidenced not only by the employee's continued employment, but also by the employer's reciprocal promise to: (i) arbitrate all claims, (ii) be bound by the arbitrator's decisions, and (iii) be responsible for any and all charges arising from the arbitration. *Flynn*, 102 F.Supp.2d at 1061. *See also, Gibson*, 121 F.3d 1126 (finding no consideration because employer failed to make promise in "Understanding" signed by employee to also submit disputes to arbitration).

C. Mutuality -- What Concessions Must An Employer Make To Enforce An Arbitration Agreement?

Courts define mutuality in very different ways; a standard approach is difficult to discern. For example, the California Supreme Court recently held that an arbitration agreement in an adhesive context, such as employment, will be unconscionable "if it requires one contracting party, but not the other, to arbitrate all claims arising out of the same transaction or occurrence or series of transactions or occurrences." *Armendariz*, 99 Cal.Rptr.2d at 772. It is unclear whether this would require an employer to submit to arbitration any claim it might wish to bring arising out of an employee's alleged breach of a confidentiality agreement, covenant not to compete, intellectual property assignment agreement, or any other similar agreement.

As a practical matter, however, an employer will not likely have a significant amount of claims against its employees, and any concern in this regard is rather speculative.

Other courts seem to address mutuality in the context of procedural fairness. For example, the Fourth Circuit has held that an arbitration agreement with the following elements was fatally flawed -- it allowed the employer, but not the employee, to bring suit in court to vacate or modify the arbitrator's award; it required the employee to list all facts supporting his claim as well as fact witnesses with a brief summary of their knowledge, but the employer did not have to supply any responsive pleadings, notice of its defenses or witness lists; the arbitrator had to be chosen from a list compiled by the employer; and, the employee could not record the arbitration hearing, although the employer was permitted to do so. *Int'l Paper Co. v. Schwabedissen Maschinen & Anlagen GMBH*, 206 F.3d 411 (4th Cir. 2000). See also, *Hooters of America, Inc. v. Phillips*, 173 F.3d 933 (4th Cir. 1999); *Gibson*, 121 F.3d 1126 (applying Indiana law, Seventh Circuit held that both parties must be bound by the terms of a contract for it to be enforceable and that the employer's failure to make a reciprocal promise to be bound by the arbitration agreement at issue resulted in a lack of consideration).

Still other courts take a much less restrictive approach. In *Wright*, 82 F.Supp.2d at 1284, the court held that the employer's promise to be bound to the arbitration process and results of disputes that are initiated **by employees** constituted sufficient consideration because the employer had agreed to arbitrate a specified class of claims -- those brought by the employees. See also, *Wilson Elec. Contractors, Inc.*

v. Minnotte Contracting Corp., 878 F.2d 167, 169 (6th Cir. 1989); *Kelly v. UHC Management Co.*, 967 F.Supp. 1240 (N.D. Ala. 1997).

D. Defenses To Enforcement Of Arbitration Agreements

In an effort to avoid mandatory arbitration after signing an arbitration agreement, employees have raised a handful of defenses to contract formation. These include unconscionability, duress, adhesion, fraudulent inducement and misrepresentation, and failure to knowingly and voluntarily waive statutory rights. *See, e.g., Great Western Mortgage Corp. v. Peacock*, 110 F.3d 222 (3d Cir. 1997) (holding that more than a disparity in bargaining power is needed to show unwillingness to enter into agreement); *Kelly*, 967 F.Supp. 1240 (holding that the knowing and voluntary standard does not apply to an agreement to arbitrate because it merely changes the forum for adjudicating statutory rights); *Walker*, 997 F.Supp. 822 (holding that there must be evidence of fraud or coercion beyond mere unequal bargaining power to find arbitration agreement unconscionable); *Flynn*, 102 F.Supp.2d 1055. While these defenses require factual inquiries on a case by case basis, courts have generally recognized the prevalent federal policy favoring arbitration and have rejected these defenses.

V. FEDERAL LAW ISSUES

A. “Due Process” Concerns⁶

Under the Supreme Court’s decision in *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), arbitration is supposed to be a reasonable substitute for a judicial forum. With this in mind, several courts have analyzed the need for arbitration agreements to provide statutory remedies and the right to representation, the proper allocation of arbitration related fees and expenses, and the extent of permissible discovery.

1. Remedies

In addressing the remedies available to an employee in arbitration, an employer’s arbitration program will pass judicial scrutiny if it provides for the same remedies that are available in a judicial forum, particularly if the employee’s claim is one based on a statutory right. For example, in *Gannon*, the court held that because the arbitration agreement failed to provide remedies equivalent to those allowed under the statutory claims at issue, it prevented the employee from effectively vindicating her rights. The statutory rights in *Gannon* were based on both federal law, Title VII, and state law, the Missouri Human Rights Act. *Gannon*, 2001 WL 930550, at *2-4 (affirming severance of arbitration agreement provision limiting punitive damages so as to permit enforcement of remainder of agreement). The

⁶ The “due process” terminology is misleading, as it implies the existence of constitutional protection to disputes against non-governmental employers. The courts’ use of the term in arbitration cases actually refers to fairness and conformity with state and federal statutes.

California Supreme Court has likewise held that, to be valid, an arbitration agreement must provide for all types of relief that would otherwise be available in court. *Armendariz*, 99 Cal.Rptr.2d at 759-60. See also, *Cole*, 105 F.3d at 1482.

2. Right to representation

If the arbitration forum is to serve as a substitute for a judicial forum, employees should clearly have the right to representation. Who should and/or can pay for the attorneys' fees is not so clear. One court invalidated that portion of an arbitration agreement intended to waive the employee's right to attorneys' fees as a prevailing party because it was inconsistent with the policy goals of Title VII. *DeGaetano v. Smith Barney, Inc.*, 1996 WL 697928 (S.D.N.Y. 1996). Compare, *Peacock*, 110 F.3d 222 (upholding an arbitration agreement that allowed representation by attorney at employee's own expense). Generally, courts will uphold a provision that requires the employer to pay reasonable attorneys' fees. Given the courts' general desire that the arbitral forum allow statutory remedies, "reasonable" attorneys' fees will most likely be those determined by an arbitrator, in essentially the same manner that judges currently consider fee applications.

3. Costs

In *Cole*, the D.C. Circuit, after a thorough analysis of the Supreme Court's holding in *Gilmer*, 500 U.S. 20, held that employers should be solely responsible for the arbitrator's fees. *Cole*, 105 F.3d at 1484. The court reasoned that employees who elect to bring their claims in federal court are not required to pay for the services of a judge. The court acknowledged that an employee may have to pay some fees:

“There is no doubt that parties appearing in federal court may be required to assume the cost of filing fees and other administrative expenses, so any reasonable costs of this sort that accompany arbitration are not problematic.” *Id.* The court also dismissed concerns that the arbitration process would become subverted by having only one party pay the arbitrator. The court stated that if an arbitrator is likely to “lean” in favor of the employer, it would be because the employer is a source of future arbitration business, not because the employer paid all of the costs. *Id.*

Additionally, in *Jones v. Fujitsu Network Communications, Inc.*, 81 F.Supp.2d 688 (N.D. Tex. 1999), the court held unenforceable a fee-splitting provision which required the employee to pay half of the arbitrator’s fees, the court reporter’s fee, the fee for the arbitrator’s copy of the transcript, and the facility costs. *See also, Shankle v. B-G Maintenance Management*, 1997 WL 416405 (D. Colo. 1997); *Baron v. Best Buy Co.*, 79 F.Supp.2d 1350 (S.D. Fla. 1999). *Compare, Chappel v. Laboratory Corp. of America*, 232 F.3d 719 (9th Cir. 2000)(upholding a cost-splitting provision in an agreement to arbitrate ERISA claims). In line with this authority, it would be reasonable for an employer to require the employee to pay a filing fee and other reasonably limited costs, but the employer should pay the arbitrator’s fees.

4. Discovery

Courts generally uphold provisions in an arbitration agreement limiting the extent of discovery, as long as they provide for more than “minimal discovery.” *Cole*, 105 F.3d at 1482. *See also, Peacock*, 110 F.3d 222 (holding that employee’s

arbitration agreement, which effectively waived the state-created right to litigation-type discovery, was enforceable under the FAA); *Armendariz*, 99 Cal.Rptr.2d at 760-61.

Similarly, an arbitrator has authority to order discovery necessary to a full and fair exploration of the issues in dispute, consistent with the expedited nature of arbitration. This may include deposition, interrogatories, document production and other methods. *American Arbitration Association National Rules For the Resolution of Employment Disputes* (attached at Tab 2).

5. Statute of Limitations

Some courts have upheld an arbitration agreement's shorter statute of limitations than was provided under the applicable law. *Soltani v. Western & Southern Life Ins. Co.*, 258 F.3d 1038 (9th Cir. 8/6/2001) (six month limitations period for wrongful discharge claims not unconscionable and thus enforceable); *Morrison v. Circuit City Stores, Inc.*, 70 F.Supp.2d 815, 827 (S.D. Ohio 1999) (holding that the one-year statute of limitations period in the arbitration agreement was fair and reasonable, even though shorter than that provided by Title VII). An Alabama district court has, however, suggested in *dicta* that if an employee's ability to vindicate his rights was hindered by the shorter statute of limitations period in the agreement, the court would modify the agreement to make it consistent with the applicable statute of limitations. *Wright*, 82 F.Supp.2d at 1288 n.5. It is noteworthy that under the American Arbitration Association's Rules, if an employee's dispute involves a statutory right, he has the same time limit to file the dispute as established

by the applicable statute of limitations. If no statutory rights are involved, then the time limit established by the arbitration agreement is followed.

B. Judicial Review

1. The FAA

Under the FAA, parties to an arbitration award can submit the award to a district court for an order confirming, modifying or correcting the award. 9 U.S.C. §13. Such judgments by the district court will have the same force and effect as a judgment in an action brought before the court. *Id.* Section 16 limits the appeals that may be taken from a court's order to those that: (i) refuse a stay of any action under section 3 of the FAA; (ii) deny a petition to order arbitration to proceed; (iii) deny an application to compel arbitration; (iv) confirm or deny confirmation of an award or partial award; or (v) modify, correct or vacate an award. *Id.* at §16.

The FAA also clearly states the circumstances under which a district court can vacate, modify or correct an arbitrator's decision. In section 10, the FAA grants a district court authority to vacate an award where the court finds corruption, fraud or undue means in the procurement of the award; partiality, corruption or misconduct on the part of the arbitrator; and, if the arbitrator exceeded his powers. *Id.* at §10. A district court may also modify or correct an award where the arbitrator makes a mistake involving a miscalculation of figures or evidence, grants an award upon a matter not submitted to him, or the award is imperfect in matter of form. *Id.* at §11. Given the Supreme Court's holding in *Southland*, 465 U.S. 1, reiterated in *Circuit*

City, 2001 WL 273205, slip op. at pp. 14-15, the FAA's provisions on judicial review would preempt any conflicting state laws.

2. Judicial review based on "manifest disregard"

In addition to the above statutory grounds for judicial review, the federal courts have recognized a judicially-created ground for modifying or vacating an arbitration award where the arbitrators engaged in "manifest disregard of the law." *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995); *DiRussa v. Dean Witter Reynolds Inc.*, 121 F.3d 818 (2d Cir. 1997), *cert. denied*, 522 U.S. 1049 (1998); *Cremin v. Merrill Lynch Pierce Fenner & Smith, Inc.*, 957 F.Supp. 1460 (N.D. Ill. 1997); *Chisolm v. Kidder, Peabody Asset Management, Inc.*, 966 F.Supp. 218 (S.D.N.Y. 1997) (holding that manifest disregard of the law doctrine requires more than error or misunderstanding with respect to the law). To modify or vacate an arbitration award on this ground, a court must find that "(1) the 'arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether,' and (2) the 'law ignored by the arbitrators . . . [was] well defined, explicit, and clearly applicable' to the case." *DiRussa*, 121 F.3d at 821 (quoting *Folkways Music Publishers, Inc. v. Weiss*, 989 F.2d 108, 112 (2d Cir. 1993)).

Additionally, the D.C. Circuit has suggested that judicial review of arbitration rulings on statutory claims should be less deferential than the limited review normally conducted in the collective bargaining context. *Cole*, 105 F.3d at 1487.

The *Cole* court observed:

The strict deference accorded to arbitration decisions in the collective bargaining arena may not be

appropriate in statutory cases in which an employee has been forced to resort to arbitration as a condition of employment. Rather, in this statutory context, the “manifest disregard of law” standard must be defined in light of the bases underlying the Court’s decision in *Gilmer* type cases.

Id. The D.C. Circuit further called for judicial review to be “sufficiently rigorous to ensure that arbitrators have properly interpreted and applied statutory law.” *Id.*

The FAA clearly limits a court’s review of the arbitrator’s award. In *Circuit City*, the Supreme Court reiterated its policy regarding arbitration previously stated in both *Gilmer* and *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985), that “‘by agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.’” *Circuit City*, 2001 WL 273205, slip op. at p.16 (*quoting Gilmer*, 500 U.S. at 26, and *Mitsubishi*, 473 U.S. at 628). Given the prevailing public policy in favor of arbitration, courts should only review arbitration decisions for legal or gross factual error. Even though the D.C. Circuit states that judicial review should be greater when statutory rights are at issue than judicial review of traditional contractual issues, *see Cole*, 105 F.3d 1465, it is unclear whether courts outside the D.C. Circuit will apply heightened scrutiny to arbitration awards that involve statutory claims. Additionally, this does not suggest that judicial review of statutory rights is a *de novo* review. *Compare, EEOC Notice, “Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment,”* No. 915.002, July 10, 1997 (stating that employers should not be “permitted to deprive civil rights claimants of the choice to

vindicate their statutory rights in the courts -- an avenue of redress determined by Congress to be essential to enforcement”).

Moreover, when a court is faced with deciding whether an issue is arbitrable, the Supreme Court has expressly favored arbitration. *See Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983). The Supreme Court stated: “Any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is in the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability.” *Id.*

C. The NLRB’s role and likely stance

The NLRB also opposes mandatory arbitration of employment disputes and has indicated that if an agreement to arbitrate prevents an employee from filing charges with the NLRB, it will find the agreement to be an unfair labor practice.⁷ *See Chisolm v. Kidder, Peabody Asset Management, Inc.*, 966 F.Supp. 218 (S.D.N.Y. 1997) (*citing* NLRB General Counsel Report, January to September 1995, Daily Lab. Rep. (BNA) No. 36, at E - 6-7 (Feb. 23, 1996)). The NLRB’s position regarding arbitration is advanced in *Bentley’s Luggage Corp.*, General Counsel Advice Memorandum, Case 12-CA-16658 (Aug. 21, 1995) (attached at Tab 4). In *Cole*, the D.C. Circuit also acknowledged the NLRB’s concerns regarding the inability of arbitration to adequately remedy employment discrimination, but upheld the arbitration agreement because it did not undermine the relevant statutory scheme.

⁷ The NLRB’s position is somewhat disingenuous; the Board has long advocated deferral to arbitration of unfair labor practice charges filed in the union setting. *Collyer Insulated Wire*, 192 N.L.R.B. 837 (1971).

105 F.3d at 1467-68. The Sixth Circuit has even indicated that an employee can effectively agree to arbitrate claims under the FLSA. *See, Floss v. Ryan's Family Steak Houses, Inc.*, 211 F.3d 306 (6th Cir. 2000), *cert. denied*, 531 U.S. 1072 (2001). *See also, Kuehner v. Dickinson & Co.*, 1996 WL 257602 (9th Cir. 1996). While the NLRB may attempt to preserve an employee's ability to file charges directly with the agency and even argue that an agreement requiring arbitration of such charges is an unfair labor practice, a reviewing court could uphold the arbitration agreement if it found that it satisfied "due process" considerations and vindicated the employee's statutory rights.

D. Preclusive effect of arbitration awards

The Supreme Court has drastically altered its position concerning whether employees have the right to pursue statutory employment law remedies in **both** an arbitral and judicial forum. In *Alexander v. Gardner-Denver Co.*, 415 U.S. 36, 47, 59-60 (1974), the Court concluded that because Title VII "vest[s] federal courts with plenary powers to enforce ..." that statute, and "specifies with precision the jurisdictional prerequisites that an individual must satisfy . . . to institute a lawsuit," an employee must be permitted "to pursue both his remedy under the grievance arbitration clause of a collective bargaining agreement and his cause of action under Title VII" which claim "the federal court should consider ... de novo."

By 1991, only four members of the unanimous Court which had decided *Gardner-Denver* remained. In *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), the Court considered whether an individual employee could waive his

right to a judicial forum over his ADEA claim. By a 7-2 majority, the Court held that a claim under the ADEA could be subjected to compulsory arbitration enforceable under the FAA. The Court found that “[a]n individual ADEA claimant subject to an arbitration agreement will still be free to file a charge with the EEOC, **even though the claimant is not able to institute a private judicial action.**” *Id.* at 28.

Thus, assuming that procedural “due process” concerns have been adequately addressed, *Gilmer* appears to have otherwise resolved whether an arbitration award involving a non-union employee will have preclusive effect on subsequent civil litigation an employee brings against his employer.

VI. FEDERAL LAW ISSUES REGARDING THE EEOC’S POSITION

A. EEOC’s opposition to mandatory arbitration agreements

The EEOC’s policy regarding mandatory arbitration agreements states “that agreements that mandate binding arbitration of discrimination claims as a condition of employment are contrary to the fundamental principles evinced in these laws.” *EEOC Notice*, “Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment,” No. 915.002, July 10, 1997 (see attached at Tab 3). The EEOC argues that Congress explicitly entrusted the primary responsibility for the interpretation, administration and enforcement of the discrimination laws to the federal government, and specifically vested in the federal courts the final responsibility for statutory enforcement through the “construction and interpretation of the statutes, the adjudication of claims, and the issuance of relief.”

Id. The EEOC further identifies inherent defects in arbitration: it prevents development of the law, it limits an employee's rights, and it maintains structural biases against employees. *Id.*

Despite the EEOC's opposition to mandatory employment arbitration agreements, courts continue to uphold them. *See, Cole*, 105 F.3d at 1468. Although the D.C. Circuit acknowledged the EEOC's concerns regarding the "potential inequities and inadequacies of arbitration in individual employment cases" and the "competence of arbitrators and the arbitral forum to enforce effectively the myriad of public laws protecting workers and regulating the workplace," it held that if an arbitration agreement does not undermine the relevant statutory scheme, the Supreme Court's decision in *Gilmer* mandates enforcement of the arbitration agreement. *Id.* at 1468-69. Because of *Gilmer*, and until either the Supreme Court overrules itself or Congress passes an amendment to the FAA, it is probable that courts will continue to enforce mandatory arbitration agreements **if** they do not undermine the relevant statutory scheme, which relates back to the "due process" considerations noted above.

B. The EEOC now has independent jurisdiction to pursue claims otherwise subject to individual arbitration agreements

The Supreme Court recently held that the EEOC lawfully may attempt to obtain monetary damages on behalf of employees covered by enforceable arbitration

agreements. *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002). This holding undercuts the effectiveness of employer/employee mandatory arbitration agreements to some extent. As discussed throughout this paper, an employee bound by an arbitration agreement will likely be precluded from filing an employment-related lawsuit against his current or former employer. However, pursuant to *Waffle House*, the EEOC may lawfully pursue a federal court action in its own name *on behalf of the employee* who is otherwise limited by an arbitration agreement.

Notwithstanding the significance of the *Waffle House* decision, given the small number of cases the EEOC currently takes to trial and the agency's limited resources, this decision will likely not have a great impact on most small to mid-size employers. Valid arbitration programs will still significantly reduce the number of employment-related lawsuits.

VII. RECOMMENDATIONS/SUGGESTED PROGRAM

In light of the above discussion and our experience with traditional labor arbitrations and employment mediations, we offer the following suggestions for employment arbitration programs:

A. Strike While The Iron Is Hot

Now is an opportune time to implement an arbitration program. Members of Congress have already proposed amending the FAA to bar prospective agreements to arbitrate employment disputes. Should control of Congress and the Presidency change, these proposals could become law. The window of opportunity for employers to utilize arbitration may thus be short-lived -- get everything you can from the process while you can.

B. Specifically Reference Major State And Federal Statutes In The Arbitration Agreement

To ensure that employees have knowingly agreed to arbitrate statutory employment claims, the agreement should reference the major statutes by name. The agreement should, however, also include broad "catch-all" language, *i.e.*, "any and all claims, including statutory claims, arising out of your employment or cessation of employment, including but not limited to...."

C. Require New Employees To Sign The Arbitration Agreement At The Outset Of Employment

New employees should be required to sign an arbitration agreement as part of the application process or following a job offer, but prior to their start dates. The refusal to sign will disqualify them from employment.

D. Advise All Current Employees Of The Decision To Implement An Arbitration Procedure, But Do Not Require Them To Sign An Agreement

The problem with requiring employees to sign an agreement to arbitrate is that many may balk. This puts the employer in the position of having to terminate

anyone who refuses (as noted earlier, this would likely beg a response from the EEOC). By implementing without a signed agreement, the employer avoids this pitfall. Moreover, several courts have indicated that a signed agreement is not necessary for enforcement. An employer would simply argue that the employees agreed to arbitration by continuing to work. If an employee attempts to sue in state or federal court, the employer could ask a federal court to stay the proceeding and enforce the arbitration agreement. Even if the federal court finds the arbitration procedure unenforceable because there was no signed agreement to arbitrate, the employer is merely left defending a suit in the usual forum -- a state or federal court. The employer could **then** choose to require signed agreements to arbitrate as a condition of continued employment.

E. Require An Employee To Pay A Filing Fee Equivalent To That He Would Have To Pay In Federal Court

This would serve as a sort of "earnest money," ensuring that employees incur some cost before pursuing their claims.

F. Appoint Arbitrators Through The AAA

We recommend using the AAA, because: (i) using a universally acknowledged neutral third party addresses many of the above due process concerns, and (ii) the AAA is getting much better at handling employment law disputes, with arbitral panels experienced in these matters. We further recommend that the employer pay the arbitral fees and expenses.

G. Consider Limiting Discovery

By far the biggest expense in employment litigation is the often protracted and unwieldy discovery process. We suggest limiting each side to one or two depositions, while affording each party the opportunity to ask the arbitrator for leave to take additional depositions, or conduct additional written discovery.

H. Consider Including A Limitations Period

Because Kentucky law allows a five year limitations period for all state civil rights and some employment related tort claims, you may wish to consider incorporating a shorter limitations period into the arbitration agreement. Some recent federal cases have affirmed the validity of shorter contractual limitations periods, which serve the important purpose of ensuring some finality to employment claims within a reasonable period after employment ends. Absent such provisions, and in light of an often transient workforce, defending years old claims is often extremely difficult.

I. Provide For Summary Judgment Proceedings

Federal courts dismiss many lawsuits in favor of employers -- a process referred to as "summary judgment." One of the primary disadvantages of arbitration programs is that arbitrators tend not to dismiss cases as readily as federal judges. However, arbitrators also tend not to award the runaway verdicts juries sometimes impose. In essence, arbitration is a form of insurance against the "big hit," while accepting the likelihood that some damages may be awarded. However, by

instituting a summary judgment procedure, that balance may be shifted more to the employer's favor.

J. Require A Transcript Of The Arbitration Hearing, Give Both Parties The Opportunity To Submit Pre-Hearing Briefs, And Require The Arbitrator To Issue A Written Opinion Containing Findings Of Fact And Conclusions Of Law

To the extent that judicial review occurs, it will only be meaningful if the parties, and the reviewing court, are provided: (i) the factual and legal rationale behind the decision, and (ii) a record of the proceedings, including a transcript and at least the opportunity to brief the issues. We also recommend that the transcript be provided to both parties at the Company's expense.

K. Provide For Confidentiality

One of the primary advantages of private arbitration is that, unlike litigation, it is not a matter of public record. Moreover, the AAA due process regime permits confidential proceedings.

L. Deny Res Judicata/Collateral Estoppel Effect To Proceedings Involving Other Employees

A corollary to confidentiality is that arbitration results are not binding in subsequent arbitrations involving different employees. Although this might have the effect of denying the Company a defense it would otherwise employ in court, it has the salutary effect of avoiding an avalanche of "me-too" claims following a successful arbitration. Employees are much less likely to choose to endure the time and trouble of arbitration if they have no certainty of success.

M. Class Action Or Joint Claims Should Not Be Permitted, Unless All Parties Agree

The risk of a substantial damages award may be unacceptably great by giving a single arbitrator the power to decide such claims. Of course, in appropriate circumstances -- particularly where the damages exposure is limited -- the Company may choose to agree to class or joint claims, as it will be more efficient to resolve all such claims in one proceeding.

N. Include A Severability Clause

An employer should include a severability clause that allows a court to “blue pencil” portions of the arbitration agreement should it find any provision unlawful. Courts will apply the rule of severability if the unlawful provisions in the agreement are not “so interdependent with the other parts of the agreement as to make them not severable.” *Wright*, 82 F.Supp. 2d 1279. For example, in *Wright*, the court concluded that a provision in the agreement limiting award of punitive damages and back/front pay could be severed in order to save the agreement. The court then provided the full range of remedies provided under the statutory law. *Id.*

VIII. POST CIRCUIT CITY CASE DIGEST

The following cases digested are Circuit Court of Appeals decisions addressing the enforceability of employer/employee arbitration agreements (and, thus, dismissal of employment-related lawsuits in favor of arbitration) in light of *Circuit City*. To the extent that the Courts’ analysis in each of these cases addresses *Circuit City*, the Federal Arbitration Act’s (“FAA”) coverage of employment-related arbitration agreements, and federal policy favoring enforcement of arbitration

agreements, the cases are quite similar. The cases differ, however, in their analysis of the validity and enforceability of the arbitration agreements at issue.

A. *Circuit City Stores, Inc. v. Ahmed*, 283 F.3d 1198 (9th Cir. 2002)

The Ninth Circuit found that, in light of the employee's meaningful opportunity to opt out of employer's binding arbitration program, which employee did not exercise, the arbitration agreement was not procedurally unconscionable and thus was enforceable.

Factual Background

One month after Mohammad S. Ahmed began working as a sales counselor for Circuit City, the company instituted an arbitration program. Each employee received a package of materials on this program, including a handbook, Circuit City's Dispute Resolution Rules and Procedures, and an "opt-out" form. Ahmed signed an acknowledgment of receipt of such package. The materials indicated an employee would be automatically part of the arbitration program and would therefore be required to arbitrate all employment-related disputes if he failed to mail the opt-out form to Circuit City within 30 days. The materials further indicated that, if an employee decided to opt-out of the arbitration program, he would be allowed to keep his job and simply not participate in the program. Ahmed did not mail in the opt-out form.

Approximately two years later, Ahmed filed suit against Circuit City in state court under the California Fair Employment and Housing Act ("FEHA"). Circuit City sought an order compelling arbitration.

Ninth Circuit Decision

The Ninth Circuit affirmed the district court's order compelling arbitration. The Ninth Circuit held the agreement to arbitrate was not procedurally unconscionable because Ahmed was given a meaningful opportunity to opt out of the agreement. Moreover, the terms of the agreement were clearly spelled out in written materials and a video presentation, Ahmed was encouraged to contact Circuit City representatives or consult an attorney prior to deciding whether to participate in the program, and he was given 30 days in which to decide whether to participate. Thus, because the arbitration agreement was not one-sided and was fairly entered-into by both Ahmed and the Company, the Ninth Circuit found it valid and enforceable.

B. *Blair v. Scott Specialty Gases*, 283 F.3d 595 (3rd Cir. 2002)

The Third Circuit found mandatory arbitration provision contained in employee handbook was supported by adequate consideration under Pennsylvania law and thus was enforceable on those grounds. However, the Court reversed and remanded to provide employee opportunity to show resort to arbitration would deny her a forum to vindicate her statutory rights, given both her financial capacity and provisions of the agreement requiring parties to each pay one-half arbitrator's compensation.

Factual Background

During Blair's employment with Scott Specialty Gases ("Scott"), an updated employee handbook was distributed to all employees. Pursuant to a provision contained in the employee handbook, Scott had a unilateral ability to modify provisions therein. However, alteration of material aspects of the handbook required written notice to employees. The handbook also contained a mandatory arbitration agreement that included a fee-sharing provision. Blair signed an acknowledgment of receipt of the handbook, acknowledging she had read the arbitration provision and agreed that she and Scott would submit any employment-related disputes to final and binding arbitration.

Approximately one year after she resigned from the company, Blair filed a complaint against Scott in federal court alleging sexual harassment, sex discrimination, and constructive discharge under Title VII, the Pennsylvania Human Relations Act ("PHRA"), and the Pennsylvania Constitution and alleging several state tort claims. Scott filed a Motion to Dismiss on the ground that Blair had agreed to submit all employment-related claims to binding arbitration. Blair, in response, argued the arbitration agreement was not a validly formed contract because it was not supported by adequate consideration. In the alternative, Blair argued the agreement should not be enforced on public policy grounds because it required her to pay one-half of the arbitrator's fees.

Third Circuit Decision

The Third Circuit held the agreement was a validly formed contract. Basing its holding on Pennsylvania contract law, the Court held the agreement was supported by adequate consideration because both Scott and Blair agreed to be bound by arbitration. The language of the arbitration clause specifically states, "if any dispute arises from your employment with Scott, *you and Scott agree* that final resolution of the dispute will occur exclusively in a final and binding arbitration proceeding." (emphasis added).

Moreover, the Third Circuit articulated, Scott's unilateral ability to alter the agreement without notice or consent did not render the agreement illusory. The company did not have an unfettered right to alter the employment agreement. Scott's right to alter the agreement was actually quite limited - it could only unilaterally make *non-material* changes to the handbook without notice or consent. The Court opined that changes to the arbitration agreement would not be categorized as non-material.

Although the Third Circuit held the agreement was a validly formed contract, the Court still remanded the case based on Blair's affidavit of her limited financial capacity and the agreement's fee-sharing provision. After an extensive analysis of an important Supreme Court decision⁸ (and other circuit court decisions) regarding the enforceability of arbitration agreements containing fee-sharing provisions, the Court determined that the court below had not allowed enough discovery to fully explore the cost issue. The Third Circuit, therefore, required that, on remand, the district court conduct limited discovery regarding the rates charged by the arbitration service, the approximate length of similar arbitration proceedings, and any other potentially relevant information. The Court reasoned that the district court will then be in a better position to determine whether resort to arbitration would deny Blair a forum to vindicate her statutory rights, given that she would have to pay one-half of the costs.

C. ***Safrit v. Cone Mills Corp.***, 248 F.3d 306 (4th Cir. 2001)

The Fourth Circuit found the collective bargaining agreement provided a clear and unmistakable waiver of employee's statutory rights to a federal forum on a Title VII claim and employee's good faith compliance with the grievance provisions of the collective bargaining agreement did not preserve the right to pursue Title VII claims in a federal forum.

Factual Background

Lori Safrit was employed at Cone Mills' plant in Salisbury, North Carolina and, during her employment, was a member of the United Needletrades, Industrial,

⁸ *Green Tree Financial Corp. -Alabama v. Randolph*, 531 U.S. 79 (2000). In this case, the plaintiff, on appeal from a district court order compelling arbitration, argued that the arbitration agreement's silence on the subject of fees created a risk that she would be required to bear a prohibitive proportion of the arbitration costs, forcing her to forego arbitration and relinquish her rights. The U.S. Supreme Court, however, held that the articulated risk to the plaintiff was too speculative to justify invalidating the arbitration agreement.

and Textile Employee Union (“UNITE”). The Collective Bargaining Agreement (“CBA”) between UNITE and Cone Mills, the agreement covering Safrit’s employment, gave the Union the *exclusive* option to proceed to arbitration. Specifically, the CBA provided a four-step grievance procedure and, if the complaint was still unresolved after the four steps, the Union could proceed to arbitration. Safrit could not proceed at any level without the Union.

In 1994, Safrit filed a grievance alleging Cone Mills failed to train her properly and denied her job opportunities because of her gender. The Union took her case to the fourth step of her grievance process. Once at the fourth step, Cone Mills agreed to correct its actions and the Union stopped pursuing the grievance. Safrit alleges, even after agreeing to correct its actions, the Company continued to discriminate against her. This time, however, the Union did not file a second grievance on her behalf. Thus, after filing a charge of discrimination with the EEOC, Safrit initiated this Title VII lawsuit against Cone Mills. Cone Mills sought dismissal of the case, arguing that the CBA clearly and unmistakably provided for arbitration as the sole remedy for alleged violations of Title VII. The company based its argument on Section XX of the CBA, which provided:

...agree that they will not discriminate against any employee with regard to race, color, religion, age, sex, national origin or disability....The parties further agreed [sic] that they will abide by all requirements of Title VII of the Civil Rights Act of 1964....Unresolved grievances arising under this section are the proper subjects of arbitration....

Fourth Circuit Decision

The Fourth Circuit held Section XX of the CBA clearly and unmistakably waived Safrit’s right to a federal forum for her Title VII claims. The Court noted that there were two ways in which a clear and unmistakable waiver can occur. First, the agreement can contain an explicit arbitration clause in which the parties agree to submit to arbitration all federal causes of action arising out of employment. Second, a general clause requiring arbitration under the agreement can be coupled with a provision which makes unmistakably clear that the employment-related statute at issue is part of the agreement. The Court then held that Section XX of the CBA clearly falls under the second of these two ways (with respect to Title VII) and, therefore, waived Safrit’s right to a federal forum on her Title VII claim.

The Fourth Circuit found Safrit’s argument, that her good faith compliance with the grievance provisions of the CBA should preserve her right to pursue claims in a federal forum, had no merit. The Court noted that, pursuant to binding Fourth Circuit case law, a collectively bargained agreement to arbitrate a statutory

discrimination on claim is enforceable. For the foregoing reasons, the Fourth Circuit affirmed the district court's grant of summary judgment to Cone Mills.

D. *Equal Employment Opportunity Commission v. Circuit City Stores, Inc.*, 285 F.3d 404 (6th Cir. 2002)

The Sixth Circuit found that employer had not presented an actual case or controversy in its action to compel former employee to arbitrate her sexual harassment dispute because employee, herself, had not sued employer.

Federal Background

As a condition to being hired by Circuit City, Julie Shelton was required to sign a form acknowledging her approval and acceptance of Circuit City's arbitration agreement. By signing the agreement, Shelton agreed to submit all her federal, state and local statutory and common-law employment-related claims to binding arbitration. Shelton signed the agreement in 1997 and was thereafter hired.

Shelton worked at Circuit City for slightly over one year. She then filed a complaint with the EEOC, claiming she had been constructively discharged as a result of sexual harassment. The EEOC subsequently filed suit against Circuit City in federal court. The Company filed a separate suit against Shelton, seeking to compel arbitration of her sexual harassment claim against the Company. Upon motion by the EEOC, the two actions were consolidated.

Sixth Circuit Decision

The Sixth Circuit affirmed the district court's decision to dismiss Circuit City's action against its former employee and ordered the Company to respond to the EEOC-initiated action. The Court premised its decision on the recent Supreme Court *Waffle House* decision. Thus, the Court found the agreement between Circuit City and Shelton, although valid and enforceable, still did not bar the EEOC from pursuing an enforcement action under Title VII on behalf of Shelton. With respect to the lawsuit filed by Circuit City against Shelton, the Court held the Company did not have a case or controversy against Shelton - Shelton did not breach her arbitration agreement with the Company because she did not file suit.

E. *Penn v. Ryan's Family Steak Houses*, 269 F.3d 753 (7th Cir. 2001)

The Seventh Circuit found the contract between the employee and arbitration service was unenforceable because it contained only an illusory promise by the

service. The Court, therefore, affirmed the district court's denial of the company's motion to compel arbitration.

Factual Background

Before Penn was employed at Ryan's Family Steak Houses ("Ryan's"), the Company had entered a contract with Employment Dispute Services, Inc. ("EDS") to have EDS provide an arbitration forum for all employment-related disputes between Ryan's and its employees. Thereafter, when Penn applied for a job at Ryan's, the Company required him to execute an arbitration agreement. The agreement was not with Ryan's; instead, Penn was required to enter this arbitration agreement with EDS.

In this agreement, EDS agreed to provide an arbitration forum for Penn in exchange for Penn's agreement to submit all employment-related disputes against Ryan's to arbitration with EDS. The agreement provided EDS with full discretion over the arbitration rules and procedures and further provided EDS with the unlimited right to modify the rules without first obtaining Penn's consent. Although Ryan's was not a party to the agreement between Penn and EDS, it was a third-party beneficiary of Penn's promise to arbitrate all of his disputes.

Penn worked as a server for Ryan's in Fort Wayne, Indiana from 1996 until 1998. After he was fired, he filed suit under The Americans With Disabilities Act ("ADA") alleging harassment and retaliation for his complaints about harassment. Ryan's filed a motion to stay the case and compel arbitration, alleging Penn was bound by the arbitration agreement he signed when he applied for his job at Ryan's.

Seventh Circuit Decision

In affirming the court below, the Seventh Circuit held that Penn never entered into an enforceable arbitration agreement. The Court noted that, under Indiana's ordinary contract principles, in order for a contract to exist, each party's promise must impose on the party a binding obligation. A party's promise fails to create a binding obligation when: (1) in effect, it promises nothing at all; (2) the party making the promise retains the right to decide whether or how to perform its promised act; or (3) the promise is so indefinite that legal enforcement would be virtually impossible.

Here, EDS promised to provide an arbitration forum in exchange for Penn's promise to submit any employment-related disputes to arbitration. EDS' promise did not impose on it a binding obligation because it retained the right to choose how it would perform its promise. Further, EDS' promise was extremely indefinite, allowing it to retain the right to modify the applicable arbitration rules and procedures without Penn's consent. Because the Court found the arbitration

agreement between EDS and Penn unenforceable, it affirmed the district court's denial of Ryan's motion to compel arbitration.

F. *Perez v. Globe Airport Security Sucs., Inc.*, 253 F.3d 1280 (11th Cir. 2001)

The Eleventh Circuit held cost-sharing provision of arbitration agreement illegal and rendered entire arbitration agreement unenforceable.

Factual Background

As a prerequisite to being hired by Globe Airport Security Sucs., Inc. ("Globe"), Perez was required to sign a "Pre-dispute Resolution Agreement" calling for the arbitration of any and all disputes relating to her employment. The Agreement expressly provided that the parties would share the fees and costs of arbitration equally. The Agreement also provided her an opportunity to consult with an attorney before signing it. However, Perez was aware she would not be considered for employment with Globe unless she signed the Agreement. She signed the Agreement and was subsequently hired.

One year after Perez's employment with Globe ended, Perez filed this law suit, alleging gender discrimination in violation of Title VII. Globe raised the arbitration agreement as an affirmative defense in its Answer. Globe then moved to compel arbitration and requested the trial court dismiss or stay the court action. Perez responded, in part, by arguing that the fee and cost-sharing provision in the arbitration agreement rendered the agreement unenforceable.

Eleventh Circuit Decision

The Eleventh Circuit affirmed the lower court's holding that the arbitration agreement's fee and cost-sharing provision rendered the entire agreement unenforceable. The court held the fee and cost-sharing provision was unenforceable because it circumscribed an arbitrator's authority to grant effective relief permitted under Title VII. The Court noted that an employee who agrees to arbitrate her statutory claims does not forego her substantive rights afforded by a statute. A substantive right afforded by Title VII is the prevailing party's right to potentially be awarded reasonable attorneys fees, including expert fees and costs. Thus, the Eleventh Circuit reasoned, because the fee and cost-sharing provision contained in this arbitration agreement prevents an employee from receiving attorneys fees and costs, it actually proscribes a substantive right afforded by Title VII. As such, the provision is illegal.

Rather than simply severing the illegal provision from the otherwise enforceable arbitration agreement, the Eleventh Circuit held the entire agreement

unenforceable. The Court acknowledged that several other courts sever illegal provisions contained in arbitration agreements either relying on a severability provision contained in the agreement or simply relying on the general federal policy in favor of enforcing arbitration. The Court, however, declined to sever the illegal provision for two reasons. First, this agreement did not contain a severability provision. Second, the Eleventh Circuit disfavors the severing of illegal provisions from otherwise enforceable arbitration agreements and chooses instead to void such agreements altogether. The Court voids such agreements because courts that will sever unlawful provisions from otherwise enforceable arbitration agreements (rather than void such agreements altogether) provide employers with incentive to continue to include unlawful provisions in their arbitration agreements. Because the Eleventh Circuit found the entire arbitration agreement unenforceable, the Court affirmed the district court's denial of Globe's motion to compel arbitration.

G. *Harden v. Roadway Package Sys., Inc.*, 249 F.3d 1137 (9th Cir. 2001)

The Ninth Circuit held that Harden, a delivery driver who signed an employment contract containing an arbitration provision, could maintain his race discrimination and wrongful termination lawsuit against Roadway Package Systems, Inc. because the FAA is inapplicable to employment contracts of drivers, like Harden, who are engaged in interstate commerce.⁹ The Ninth Circuit, therefore, found the district court lacked the authority to compel arbitration.

H. *Horenstein v. Mortgage Market, Inc.*, 2001 WL 502010 (9th Cir. 2001)

Despite appellants' argument that the arbitration clauses contained in their employment agreements should not be enforced because they eliminate the employee's right to process as a class action, the Ninth Circuit found employees' Fair Labor Standard Act ("FLSA") claims were subject to arbitration. The court,

⁹ Section 1 of the FAA provides "nothing herein contained shall apply to contracts of employment of seamen, railroad employees or any other class of workers engaged in foreign or interstate commerce." 9 U.S.C. §1. As a delivery driver for Roadway, Harden contracted to deliver packages throughout the United States, with connecting international service. Thus, he engaged in interstate commerce that is exempt from the FAA.

therefore, affirmed the district court's grant of employer's motion to compel arbitration.

The Ninth Circuit found the employees' contention, that the arbitration clause in their employment agreements should not be enforced because it eliminates their statutory right to a collective action, insufficient to render the arbitration clause unenforceable. The Court first looked to the text of the FLSA, its legislative history, and the arbitration clause and found nothing indicating that Congress intended to preclude arbitration of FLSA claims. The Court then acknowledged that plaintiffs who sign arbitration agreements lack the procedural right to proceed as a class. However, it noted that these plaintiffs nonetheless retain all substantive rights under the statute. Further, the Court cited Supreme Court precedent in concluding that only those who consent to binding arbitration agreements are forced to abandon class action. The employees here knowingly signed valid agreements to arbitrate their statutory claims; accordingly, they abandoned their right to enforce those claims as part of a class action. For the reasons described herein, the Ninth Circuit held the employees' FLSA claims are subject to arbitration and affirmed the district court's grant of the Company's motion to compel arbitration.

**UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF KENTUCKY
LOUISVILLE DIVISION
CIVIL ACTION NO. 3:97-CV-497-R**

DAVID STEPHEN BROWN, *et. al.*

PLAINTIFFS

vs.

J.C. PENNEY CO., INC., *et. al.*

DEFENDANTS

MEMORANDUM OPINION

This matter is before the court upon motions submitted by the parties. For the reasons that follow, Plaintiffs' motions to remand to the Jefferson Circuit Court and to stay proceedings pending this Court's ruling on the motion to remand are DENIED; Defendants' motion to dismiss Defendants Weidle, Walters, and O'Brien is GRANTED; and Defendant's motion to stay proceedings regarding Plaintiff Brown pending arbitration is GRANTED.

I. FACTS AND CLAIMS

Plaintiffs are former employees of Defendant J.C. Penney. Plaintiffs claim that their employment with Defendant J.C. Penney was terminated based upon their medical disabilities, in violation of the Kentucky Civil Rights Act, Ky.Rev.Stat. Ch. 344. (Complaint, Dkt. # 1). No federal claim has been asserted. Plaintiff Brown suffered from a knee injury, and Plaintiff Matthis suffered from epilepsy. Plaintiffs claim that their employment was terminated in order for Defendant J.C. Penney to save on health care expenses. Defendants Weidle, Walters, and O'Brien were supervisors of Plaintiffs during their employment with Defendant J.C. Penney.

This action was removed under 28 U.S.C. § 1441 from the Jefferson Circuit Court on July 3, 1997. Defendant J.C. Penney asserts that this Court has subject matter jurisdiction based

on diversity of the parties under 28 U.S.C. § 1332. Plaintiffs and Defendants Wiidle, Walters, and O'Brien are all Kentucky residents. Defendant J.C. Penney claims that the individually named Defendants have been fraudulently joined and, thus, the individually named Defendants should be dismissed, and this Court has subject matter jurisdiction over the remaining action.

The motion to stay proceedings pending mandatory arbitration applies only to Plaintiff David S. Brown. Plaintiff Brown was employed as a "Loss Prevention Manager" by J.C. Penney. Defendant claims that Plaintiff must arbitrate his claim under the so-called "JCPenney Alternative" Program ("Program"). Employees hired or promoted into a position covered by the Program after March 1, 1996, were required to sign an agreement which stated that adherence to the Program was a condition to employment. Those already holding covered positions at the time of implementation were not made to sign such an agreement. However, they were given materials which, after explaining the Program, stated,

The JCPENNEY ALTERNATIVE will be expanded to remaining General Management and all Store Management associates. You and JCPenney are required to use this program. In the future, if you feel you have been unlawfully terminated, you must use THE JCPENNEY ALTERNATIVE program, rather than courtroom litigation to resolve differences regarding that termination.

Dkt. # 5, Defendant's Exhibit #1, at 9. Covered employees were also shown a video tape explaining the program. Defendant asserts that Plaintiff agreed to abide by the arbitration program by continuing his employment. Plaintiff contends that further discovery is necessary to determine whether there was a sufficient "meeting of the minds" for these acts to constitute a contract.

II. FRAUDULENT JOINDER

The Sixth Circuit has established that the burden to establish federal jurisdiction is on the removing party and that the "removing party bears the burden of demonstrating fraudulent joinder." *Alexander v. Electronic Data Systems*, 13 F.3d 940, 948-49 (6th Cir. 1994). The Court recognized that,

[t]here can be no fraudulent joinder unless it be clear that there can be no recovery under the law of the state on the cause alleged or on the facts in view of the law. . . . One or the other at least would be required before it could be said that there was no real intention to get a joint judgment, and that there was no colorable ground for so claiming.

Id. at 949 quoting *Bobby Jones Garden Apartments, Inc. v. Suleski*, 391 F.2d 172, 176 (5th Cir. 1968).

The Court established that the ambiguities should benefit the party moving for remand.

“[A]ny disputed questions and fact ambiguities and ambiguities in the controlling state law [should be resolved] in favor of the nonremoving party.” *Id. quoting Carriere v. Sears Roebuck & Co.*, 893 F.2d 98, 100 (5th Cir. 1990)

Defendants claim that Defendants Weidle, Walters, and O’Brien claim were fraudulently joined because there is no individual liability for supervisors under Kentucky civil rights laws. Kentucky courts have not addressed this issue.

Ky.Rev.Stat. 344.020(1)(a) states that purpose of the Kentucky Civil Rights Act is to “provide for execution within the state of the policies embodied in [Federal Civil Rights laws.] Therefore, Kentucky courts often look to federal law in interpreting the Kentucky Act. *See Palmer v. International Ass’n of Machinists*, 882 S.W.2d 117 (Ky. 1994); *White v. Rainbo Baking Co.*, 765 S.W.2d 26 (Ky.Ct.App. 1988) Despite Plaintiffs’ assertions that remand is appropriate because Kentucky Courts have not ruled on this issue, it is clear that it is appropriate to look at federal interpretations of the Kentucky Act.

It is well established that there is no individual liability for supervisors under Title VII. *Wathen v. General Electric Co.*, 115 F.3d 400 (6th Cir. 1997). The Sixth Circuit has held that the substantive legal analysis for claims asserted against individual supervisors is the same under Title VII and the Kentucky Civil Rights Act. *Id.* at 404. Other Federal District Courts have denied remand to state courts in situations identical to the case at bar. *Woodrum v. Lane Bryant the Limited, Inc.*, 964 F.Supp. 243 (W.D. Ky. 1997).

In response, Plaintiffs claim that the individually named Defendants can be held liable under a conspiracy theory based upon Ky.Rev.Stat. 344.280. However, that statute creates a cause of action for someone who was retaliated against for exercising their civil rights. Plaintiffs in this case present no allegations of a conspiracy for such retaliation.

Based on the Sixth Circuit’s holding in *Alexander*, this Court need only find a “reasonable basis for predicting that state law might impose liability on the facts involved.” 13 F.3d at 949, *quoting Carriere v. Sears Roebuck & Co.*, 893 F.2d 98, 100 (5th Cir. 1990) However, based upon the Sixth Circuit’s clear rejection of liability for individual supervisors under the Kentucky Civil Rights Act, there is no such reasonable basis in the current case.

Therefore, the individual Defendants must be dismissed from this action. Without the individually named Defendants, this Court has subject matter jurisdiction over this action based on diversity under 28 U.S.C. § 1332 and the motion to remand to the Jefferson Circuit Court must be denied.

III. ARBITRATION

A. APPLICATION OF FAA TO EMPLOYMENT CONTRACTS

The federal Arbitration Act, 9 U.S.C. §§ 1 et seq. ("FAA"), mandates that suits pending in federal courts regarding matters covered by a contractual arbitration clause must be stayed pending such arbitration. The FAA states,

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

9 U.S.C. § 3.

Pursuant to this section, Defendant J.C. Penney has filed a motion to stay proceedings pending arbitration. Plaintiff Brown claims that the FAA does not apply to this case for a number of reasons.

1. Exception for seamen, railroad employees, or any other class of worker engaged in foreign or interstate commerce,

The FAA does not apply to "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." *Id.* at § 1. A minority of jurisdictions have applied this exception to all employment contracts. *Slawsky v. True Form Foundations*, 1991 WL 98906 (E.D.Pa. 1991) However, the weight of case law takes a narrow view of this exception.

The Supreme Court has held that federal statutory employment-related claims are subject to resolution by mandatory arbitration where there is no law specifically prohibiting arbitration. *Gilmer v. Interstate Johnson Lane Corp.*, 500 U.S. 20 (1991). In *Gilmer*, the Court held that a financial services manager must arbitrate his age discrimination claim against his employer because he had signed a securities registration application which mandated such arbitration. The Court determined that it did not have to determine whether the FAA applied to employment disputes because the contract in that case was with a trade association.

The Sixth Circuit has adopted a very narrow interpretation of the § 1 exemption in *Asplundh Tree Expert Company v. Bates*, 71 F.3d 592 (6th Cir. 1995). The *Bates* Court

concluded that “the exclusionary clause of § 1 of the Arbitration Act should be narrowly construed to apply to employment contracts of seamen, railroad workers, and any other class of workers actually engaged in the movement of goods in interstate commerce in the same way that seamen and railroad workers are.” *Id.* at 600-01

The Court did acknowledge that the employee in *Bates* was a highly paid employee, “the arbitration clause is contained in an employment contract between a highly paid executive and his corporate employer. The parties included in their bargain an agreement that any disputes would be resolved by arbitration.” 71 F.3d at 602. However, there is nothing in the decision which indicates that the bargaining position of the employee is relevant to the enforceability of the contract provision.

2. “Maritime” or “Transaction Involving Commerce” Requirement

The FAA applies to “a written provision in any maritime transaction or contract evidencing a transaction involving commerce . . .” 9 U.S.C. § 2. Plaintiff interprets this provision to mean that the FAA only applies to contracts directly involving a “transaction involving commerce.” Plaintiff relies on *Rushton v. Meijer, Inc.*, 225 Mich.App. 150 (available at 1997 WL 476366 (Mich.App.)), for this proposition. Based upon *Rushton*, Plaintiff asserts that the FAA does not apply to the current case because the employment contract in question does not directly involve commerce. The Michigan state court’s decision, however, is contradicted by the weight of federal case law.

The Supreme Court has stated that the “commerce” requirement should be viewed “not as an inexplicable limitation on the power of the federal courts, but as a necessary qualification on a statute intended to apply in state and federal courts.” *Southland Corp. v. Keating*, 465 U.S. 1, 14 (1984). The Sixth Circuit has acknowledged that under *Keating*, “§ 2 gives [the FAA] as a whole the same reach as Congress’s commerce clause power.” *Asplundh Tree Expert Co. v. Bates*, 71 F.3d 592, 600 (6th Cir. 1995) quoting *DiCrisci v. Lyndon Guaranty Bnk.*, 807 F.Supp. 947, 953 (W.D.N.Y. 1992).

While the exception for employment contracts for any “class of workers engaged in foreign or interstate commerce” has been narrowly interpreted, it is clear that the scope of the FAA itself is the equivalent to the broad scope of the commerce clause.

3. State Constitutional Protections

Plaintiff claims that he should be able to proceed with the current action despite the alleged arbitration agreement because of the protections of the Kentucky Constitution. However, the U.S. Supreme Court has held that the FAA preempts state law. The Supreme Court has stated that “[i]n § 2 of the [FAA], Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of

claims which the contracting parties agreed to resolve by arbitration. *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984) In *Perry v. Thomas*, 482 U.S. 483 (1987), the Court held that § 2 of the FAA preempted § 229 of the California Labor Code, which provided that actions for the collection of wages may be maintained "without regard to the existence of any private agreement to arbitrate." *Id.*

The Sixth Circuit has compelled arbitration of discrimination claims under state and federal civil rights laws and state contract law in *Willis v. Dean Witter Reynolds, Inc.*, 948 F.2d 305 (6th Cir. 1991) In *Willis*, the Plaintiff had signed the same type of securities registration application that was in issue in *Gilmer*. She brought suit under Ky.Rev.Stat. § 344.040, Title VII, and common law claims of outrage and breach of contract. The district court compelled arbitration on the contract claims, but denied the motion to compel the civil rights claims. The Sixth Circuit reversed the district court's denial.

Plaintiff's assertion that contractual rights do not consume one's statutory right to bring a civil rights action confuses the real issue in this case. While the existence of a contractual cause of action does not prevent a claimant from asserting a statutory cause of action, the existence of a federal statute mandating arbitration does preempt state statutory or constitutional claims.

Based upon the Sixth Circuit's holding in *Bates*, this Court must apply the FAA to employment contracts. It is clear that Defendant's employees who signed employment contracts which stated that adherence to the Program was a condition to employment would be bound by that agreement. Therefore, the question becomes whether Brown's receipt of the materials describing the program constitutes an enforceable employment contract in the absence of a writing signed by the parties.

B. APPLICATION OF FAA TO IMPLIED EMPLOYMENT CONTRACTS

1. Writing Requirement Under the FAA

Plaintiff asserts that there is no enforceable contract in this case because there is no writing signed by both parties. Again, the FAA applies to a "written provision in any maritime transaction or contract evidencing a transaction involving commerce" 9 U.S.C. § 2. Plaintiff fails to offer any authority that the FAA only applies to written contracts signed by the parties. A number of federal cases have determined that while the FAA requires a writing, "it does not require that the writing be signed by the parties." *Genesco, Inc. v. Kakiuchi & Co., Ltd.*, 815 F.2d 840, 846 (2d Cir. 1987) citing *Medical Development Corp. v. Industrial Molding Corp.*, 479 F.2d 345, 348 (10th Cir. 1973).

Plaintiff does not dispute that he received documents explaining the J.C.Penney Alternative prior to the effective date of the program. Therefore the writing requirement is satisfied.

2. Consideration for Modification of Employment Contracts

The Kentucky Supreme Court has indicated that continued employment is sufficient consideration for modification of an employment contract. *Higdon Food Service, Inc. v. Walker*, 641 S.W.2d 750 (Ky. 1982) In *Higdon*, an employee had worked for a wholesale grocery company for four years with no written employment contract. All employees were then required to sign an anti-compete agreement, arguably with no consideration to themselves. The Court held that the contract signed by the employees was the equivalent of a "new employment" and stated "[t]he hiring itself (or rehiring, if one prefers that word) was sufficient consideration for the conditions agreed to by [the employee]" *Id.* at 751

Higdon strongly indicates that under Kentucky law, continued employment is sufficient consideration for modification of an employment contract.¹ Therefore, the question becomes whether an employer can impose a binding employment contract on existing employees absent a signed contract.

3. Creation of Implied Employment Contracts in Kentucky

A federal court in Kentucky has found that while "Kentucky courts have not specifically addressed the requirements for creating an implied employment contract. . . . They have held that the at-will employment relationship may be modified, without additional consideration if the employer clearly states an intention to do so." *Hines v. Elf Atochem North America, Inc.*, 813 F.Supp. 550 (W.D. Ky. 1993) *citing Shah v. American Synthetic Rubber Corp.*, 655 S.W.2d 489 (Ky. 1983). The Court concluded "that in certain circumstances the Kentucky Supreme Court will treat employment manuals or other statements of policy as contracts binding on the employer." *Id.* at 552 The Court held that the employer's posting of rules of conduct could be construed as creating an implied employment contract and thus denied the employer's motion to dismiss the claim for breach of an implied contract. *Id.* at 553. If such an implied contract is binding on the employer, it must be binding on the employee.

Based on this case law, it appears that Kentucky general contract law would find an implied employment contract where the employer notifies the employee of a change in policy and the employee continues working.

There is no dispute that Plaintiff received the materials explaining the program. Therefore, the Court must determine whether the language of the materials given to Plaintiff are sufficient, as a matter of law, to put the employee on notice of a change in his employment terms.

¹ However, the Court did find in the alternative that the employee did receive consideration because the new contract indicated that he could only be discharged for good cause as opposed to "at will". 641 S.W.2d at 752.

4. Implied Employment Contract as a Matter of Law

Plaintiff asserts that the existence of a contract is a fact question for the jury, and Plaintiff correctly asserts that there was no question of whether a contract existed in the cases cited by Defendant that enforced the FAA. Plaintiff claims that further discovery is necessary to determine whether Plaintiff Brown agreed to the arbitration provision as a condition of continued employment, and thus, whether there was a sufficient "meeting of the minds" to form a contract.

Plaintiff cites to *Hathaway v. Gen'l Mills, Inc.*, 711 S.W.2d 227 (Tex. 1986), in which the Texas Supreme Court held that in order for an employment contract modification to be effective, "an employer asserting modification must prove that he unequivocally notified the employee of definite changes in employment terms." *Id.* at 229. The Texas court also held that once notice is proven, the employee's continued employment was proof of the employee's acceptance of the modification. The *Hathaway* Court found that there was an issue of fact in that case because the parties told different versions of what the employee was told. In the case at hand, there is no dispute whether Plaintiff Brown received the above quoted materials.

Plaintiff also cites to *Barger v. Gen'l Electric Co.*, 599 F.Supp. 1154 (W.D. Va. 1984) for the proposition that while an employment contract may be modified and continuing to work may be considered acceptance of the changes, the question of whether there was a contract, as well as the terms of the alleged contract, were "triable issues of fact." The Court interpreted Virginia employment law as follows:

First, an employer may make several different promises in addition to a promise of salary in exchange for the employee's single promise to faithfully render his services; there is no failure of consideration so long as both parties have made some obligation. Second, an employer can contractually surrender his power to terminate at-will. Even if the employee can still quit at will, the contract is not void for lack of consideration; there is no requirement of complete mutuality of obligation. Third, an employee's continued service and his failure to exercise his power to terminate his employment is sufficient consideration for an additional promise by the employer which modifies the terms of the employment contract.

Id. The *Barger* court remanded the proceedings to determine whether the employee handbook could be enforced against the employer as an employment contract.

A Federal District Court in South Carolina has ruled on a case nearly identical to the current case in *Reese v. Commercial Credit Corporation*, 955 F.Supp. 567 (D.S.C. 1997). The court, applying South Carolina general contract law, found that the employee's continued employment after receiving notice of the employer's change in policy requiring arbitration for wrongful termination claims constituted a valid employment contract. *Id.*

Plaintiff distinguishes Reese by claiming that Kentucky Constitutional protections make application of South Carolina general contract law inapplicable. However, since the FAA preempts Kentucky Constitutional protections, such protections against arbitration should not be considered when looking at general contract law in Kentucky for purposes of whether there was a binding implied contract in this situation. In other words, it is not enough to claim that Kentucky general contract law would not recognize an arbitration provision in this situation because the FAA states that such provisions are not invalid as a matter of law. In order to invalidate the provision, Plaintiff would have to demonstrate that the contract is invalid for a reason beyond the mere inclusion of an arbitration provision.

Plaintiff cites to *The Prudential Insur. Co. of America v. Lai*, 42 F.3d 1299 (9th Cir. 1993) where the Ninth Circuit determined that a signed securities exchange form mandating arbitration did not apply to a sexual discrimination claim against the claimant's employer. The Court concluded that "a Title VII plaintiff may only be forced to forego her statutory remedies and arbitrate her claims if she has knowingly agreed to submit such suits to arbitration." *Id.* at 1305. The court held that since the form signed by the plaintiff "did not purport to describe the types of disputes that were to be subject to arbitration," the plaintiff did not knowingly forego her statutory remedies and could not be forced to arbitrate her sexual discrimination claim. *Id.*

Unlike in *Lai*, the language of the materials provided by Defendant J.C. Penney clearly described the types of disputes that were to be subject to arbitration. The materials received by Plaintiff stated, "if you feel you have been unlawfully terminated, you must use the JCPENNEY ALTERNATIVE program [mandatory arbitration], rather than courtroom litigation to resolve differences regarding that termination."

Based on this weight of authority, it is clear that the materials received by Plaintiff are sufficient to establish an implied employment contract as a matter of law. This contract includes a provision calling for mandatory arbitration of employment disputes, therefore, the FAA must be applied, and the litigation regarding Plaintiff Brown must be stayed pending such arbitration.

C. PUBLIC POLICY

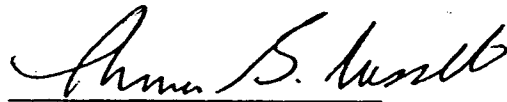
While there appears to be some legitimate public policy concerns regarding the ability of an employer to force an employee to contract away constitutional and statutory rights, the overwhelming weight of authority discounts such public policy concerns. Mandatory arbitration merely denies immediate access to the courts, it does not deny the substance of the underlying claim. The Supreme Court has noted that plaintiffs who arbitrate their statutory claims do not "forego the substantive rights afforded by the statute." *Mitsubishi Motors*, 473 U.S. at 628, 105 S.Ct. at 3354. The FAA provides a remedy should the arbitration proceedings not be conducted fairly. 9 U.S.C. § 10.

Given the weight of case law enforcing the FAA in these situations, and the U.S.

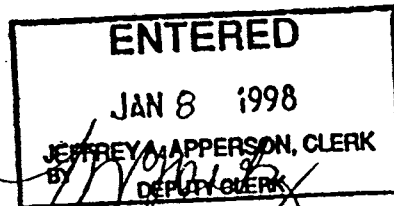
Supreme Court's encouragement of arbitration under the FAA, any such public policy arguments against mandatory arbitration ultimately fail.

The Sixth Circuit has determined that the FAA applies to most employment contracts that contain such a clause. The FAA preempts state constitutional protections. While there was no expressly bargained for signed contract in the case at hand, Kentucky case law indicates that the terms imposed upon J.C.Penney's employees were contractually effective. Therefore, J.C.Penney's motion to stay proceedings pending arbitration must be granted.

An appropriate order shall issue.



Thomas B. Russell, Judge
United States District Court





Rules and Procedures

Rules

National Rules for the Resolution of Employment Disputes

(Including Mediation and Arbitration Rules)

As Amended and Effective on January 1, 2001

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MEDIATION FEE SCHEDULE

Introduction

Federal and state laws reflecting societal intolerance for certain workplace conduct, as well as court decisions interpreting and applying those statutes, have redefined responsible corporate practice and employee relations. Increasingly, employers and employees face workplace disputes involving alleged wrongful termination, sexual harassment, or discrimination based on race, color, religion, sex, national origin, age and disability.

As courts and administrative agencies become less accessible to civil litigants, employers and their employees now see alternative dispute resolution ("ADR") as a way to promptly and effectively resolve workplace disputes. ADR procedures are becoming more common in contracts of employment, personnel manuals and employee handbooks. Increasingly, corporations and their employees look to the American Arbitration Association as a resource in developing prompt and effective employment procedures for employment-related disputes.

These rules have been developed for employers and employees who wish to use a private alternative to resolve their disputes, enabling them to have complaints heard by an impartial person with expertise in the employment field. These procedures benefit both the employer and the individual employee by making it possible to resolve disputes without extensive litigation.

Role of the American Arbitration Association

The American Arbitration Association, founded in 1926, is a not-for-profit, public service organization dedicated to the resolution of disputes through mediation, arbitration, elections, and other voluntary dispute resolution procedures. Over 4,000,000 workers are now covered by employment ADR plans administered by the AAA.

In addition, the AAA provides education and training, specialized publications, and research on all forms of dispute settlement. With 36 offices nationwide and cooperative agreements with arbitral institutions in 38 other nations, the American Arbitration Association is the nation's largest private provider of ADR services.

For seventy-five years, the American Arbitration Association has set the standards for the development of fair and equitable dispute resolution procedures. The development of the National Rules for the Resolution of

Employment Disputes, and the reconstitution of a select and diverse roster of expert neutrals to hear and resolve disputes, are the most recent initiatives of the Association to provide private, efficient and cost-effective procedures for out-of-court settlement of workplace disputes.

Legal Basis of Employment ADR

Since the beginning of this decade, Congress has twice reaffirmed the important role of ADR in the area of employment discrimination - in the Americans with Disabilities Act in 1990, and a year later in Section 118 of the Civil Rights Act in 1991. While technically not dealing with a contract of employment, the seminal court case dealing with the arbitration of disputes relating to the non-union workplace is *Gilmer v. Interstate/Johnson Lane*, 500 U.S. 20, 111 S.Ct. 1647 (1991). The Supreme Court refused to invalidate *Gilmer's* agreement with the New York Stock Exchange that he would arbitrate disputes with his employer (*Interstate/Johnson Lane*) simply because he was obliged to sign it in order to work as a securities dealer whose trades were executed on the Exchange. Although the *Gilmer* Court found that the Age Discrimination in Employment Act did not preclude arbitration of age discrimination claims, it specifically declined to decide whether employment arbitration agreements were the type of "contracts of employment" which are not made enforceable by the Federal Arbitration Act.

Since *Gilmer*, lower federal courts have generally enforced employer-imposed ADR programs, as long as the programs are fair. Some courts have held that the employee must have received adequate notice of the program. However, the issue of binding arbitration programs that are a condition of employment is still giving rise to litigation.

The Fairness Issue: The Due Process Protocol

The Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship was developed in 1995 by a special task force composed of individuals representing management, labor, employment, civil rights organizations, private administrative agencies, government, and the American Arbitration Association. The Due Process Protocol, which was endorsed by the Association in 1995, seeks to ensure fairness and equity in resolving workplace disputes. The Due Process Protocol encourages mediation and arbitration of statutory disputes, provided there are due process safeguards. It conveys the hope that ADR will reduce delays caused by the huge backlog of cases pending before administrative agencies and the courts. The Due Process Protocol "recognizes the dilemma inherent in the timing of an agreement to mediate and/or arbitrate statutory disputes" but does not take a position on whether an employer can require a pre-dispute, binding arbitration program as a condition of employment.

The Due Process Protocol has been endorsed by organizations representing a broad range of constituencies. They include the American Arbitration Association, the American Bar Association Labor and Employment Section, the American Civil Liberties Union, the Federal Mediation and Conciliation Service, the National Academy of Arbitrators, and the National Society of Professionals in Dispute Resolution. The National Employment Lawyers Association has endorsed the substantive provisions of the Due Process Protocol. It has been incorporated into the ADR procedures of the Massachusetts Commission Against Discrimination (MCAD) and into the Report of the United States Secretary of Labor's Task Force in Excellence in State and Local Government.

AAA's Employment ADR Rules

On June 1, 1996, the Association issued National Rules for the Resolution of Employment Disputes. The rules reflected the guidelines outlined in the Due Process Protocol and were based upon the AAA's California Employment Dispute Resolution Rules, which were developed by a committee of employment management and plaintiff attorneys, retired judges and arbitrators, in addition to Association executives. The revised rules were developed for employers and employees who wish to use a private alternative to resolve their disputes. The rules enabled parties to have complaints heard by an impartial person of their joint selection, with expertise in the employment field. Both employers and individual employees benefit by having experts resolve their disputes without the costs and delay of litigation. The rules included procedures which ensure due process in both the mediation and arbitration of employment disputes. After a year of use, the rules have been amended to address technical issues.

AAA's Policy on Employment ADR

The AAA's policy on employment ADR is guided by the state of existing law, as well as its obligation to act in an impartial manner. In following the law, and in the interest of providing an appropriate forum for the resolution of employment disputes, the Association administers dispute resolution programs which meet the due process standards as outlined in its National Rules for the Resolution of Employment Disputes and the Due Process Protocol. If the Association determines that a dispute resolution program on its face substantially and materially deviates from the minimum due process standards of the National Rules for the Resolution of Employment Disputes and the Due Process Protocol, the Association may decline to administer cases under that program. Other issues will be presented to the arbitrator for determination.

Notification

If an employer intends to utilize the dispute resolution services of the Association in an employment ADR plan, it shall, at least thirty (30) days prior to the planned effective date of the program: (1) notify the Association of its intention to do so; and (2) provide the Association with a copy of the employment dispute resolution plan. If an employer does not comply with this requirement, the Association reserves the right to decline its administrative services. Copies of all plans should be sent to the American Arbitration Association's Office of Program Development, 335 Madison Avenue, New York, NY 10017; FAX: 212-716-5913.

Designing an ADR Program

The guiding principle in designing a successful employment ADR system is that it must be fair in fact and perception. The American Arbitration Association has considerable experience in administering and assisting in the design of employment ADR plans, which gives it an informed perspective on how to effectively design ADR systems, as well as the problems to avoid. Its guidance to those designing employment ADR systems is summarized as follows:

- The American Arbitration Association encourages employers to consider the wide range of legally available options to resolve workplace disputes outside the courtroom.
- A special emphasis is placed by the Association on encouraging the development of in-house dispute resolution procedures, such as open door policies, ombuds, peer review, and internal mediation.
- The Association recommends an external mediation component to resolve disputes not settled by the internal dispute resolution process.
- Programs which use arbitration as a final step may employ:
 - pre-dispute, voluntary final and binding arbitration;
 - pre-dispute, mandatory nonbinding arbitration;
 - pre-dispute, mandatory final and binding arbitration; or
 - post-dispute, voluntary final and binding arbitration.
- Although the AAA administers binding arbitration systems that have been required as a condition of initial or continued employment, such programs must be consistent with the Association's National Rules for the Resolution of Employment Disputes and the Due Process Protocol.

Specific guidance on the responsible development and design of employment ADR systems is contained in the Association's publication, *Resolving Employment Disputes: A Practical Guide*, which is available from any AAA office.

Alternative Dispute Resolution Options

Open Door Policy: Employees are encouraged to meet with their immediate manager or supervisor to discuss problems arising out of the workplace environment. In some systems, the employee is free to approach anyone in the chain of command.

Ombuds: A neutral third party (either from within or outside the company) is designated to confidentially investigate and propose settlement of employment complaints brought by employees.

Peer Review: A panel of employees (or employees and managers) works together to resolve employment complaints. Peer review panel members are trained in the handling of sensitive issues.

Internal Mediation: A process for resolving disputes in which a neutral third person from within the company, trained in mediation techniques, helps the disputing parties negotiate a mutually acceptable settlement. Mediation is a nonbinding process in which the parties discuss their disputes with an impartial person who assists them in reaching a settlement. The mediator may suggest ways of resolving the dispute but may not impose a settlement on the parties.

Fact-Finding: The investigation of a complaint by an impartial third person (or team) who examines the complaint and the facts and issues a non-binding report. Fact-finding is particularly helpful for allegations of sexual harassment, where a fact-finding team, composed of one male and one female neutral, investigates the allegations and presents its findings to the employer and the employee.

Arbitration: Arbitration is generally defined as the submission of disputes to one or more impartial persons for final and binding determination. It can be the final step in a workplace program that includes other dispute resolution methods. There are many possibilities for designing this final step. They include:

Pre-Dispute, Voluntary Final and Binding Arbitration: The parties agree in advance, on a voluntary basis, to use arbitration to resolve disputes and they are bound by the outcome.

Pre-Dispute, Mandatory Nonbinding Arbitration: The parties must use the arbitration process to resolve disputes, but they are not bound by the outcome.

Pre-Dispute, Mandatory Final and Binding Arbitration: The parties must arbitrate unresolved disputes and they are bound by the outcome.

Post-Dispute, Voluntary Final and Binding Arbitration: The parties have the option of deciding whether to use final and binding arbitration after a dispute arises.

Types of Disputes Covered

The dispute resolution procedures contained in this booklet can be inserted into an employee personnel manual, an employment application of an individual employment agreement, or can be used for a specific dispute. They do not apply to disputes arising out of collective bargaining agreements.

NATIONAL RULES FOR THE RESOLUTION OF EMPLOYMENT DISPUTES

1. Applicable Rules of Arbitration

The parties shall be deemed to have made these rules a part of their arbitration agreement whenever they have provided for arbitration by the American Arbitration Association (hereinafter "AAA") or under its National Rules for the Resolution of Employment Disputes. If a party establishes that an adverse material inconsistency exists between the arbitration agreement and these rules, the arbitrator shall apply these rules.

If, within thirty (30) days after the Association's commencement of administration, a party seeks judicial intervention with respect to a pending arbitration, the Association will suspend administration for sixty (60) days to permit the party to obtain a stay of arbitration from the court.

These rules, and any amendment of them, shall apply in the form obtaining at the time the demand for arbitration or submission is received by the AAA.

2. Notification

An employer intending to incorporate these rules or to refer to the dispute resolution services of the AAA in an employment ADR plan, shall, at least thirty (30) days prior to the planned effective date of the program:

- i) notify the Association of its intention to do so and,
- ii) provide the Association with a copy of the employment dispute resolution plan.

Compliance with this requirement shall not preclude an arbitrator from entertaining challenges as provided in Section 1. If an employer does not comply with this requirement, the Association reserves the right to decline its administrative services.

3. AAA as Administrator of the Arbitration

When parties agree to arbitrate under these rules, or when they provide for arbitration by the AAA and an arbitration is initiated under these rules, they thereby authorize the AAA to administer the arbitration. The authority and duties of the AAA are prescribed in these rules, and may be carried out through such of the AAA's representatives as it may direct.

4. Initiation of Arbitration

Arbitration shall be initiated in the following manner.

- a. The parties may submit a joint request for arbitration.

b. In the absence of a joint request for arbitration:

(i) The initiating party (hereinafter "Claimant[s]") shall:

- (1) File a written notice (hereinafter "Demand") of its intention to arbitrate at any regional office of the AAA, within the time limit established by the applicable statute of limitations if the dispute involves statutory rights. If no statutory rights are involved, the time limit established by the applicable arbitration agreement shall be followed. Any dispute over such issues shall be referred to the arbitrator. The filing shall be made in duplicate, and each copy shall include the applicable arbitration agreement. The Demand shall set forth the names, addresses, and telephone numbers of the parties; a brief statement of the nature of the dispute; the amount in controversy, if any; the remedy sought; and requested hearing location.
- (2) Simultaneously mail a copy of the Demand to the party (hereinafter "Respondent[s]").
- (3) Include with its Demand the applicable filing fee, unless the parties agree to some other method of fee advancement.

(ii) The Respondent(s) shall file an Answer with the AAA within ten (10) days after the date of the letter from the AAA acknowledging receipt of the Demand. The Answer shall provide the Respondent's brief response to the claim and the issues presented. The Respondent(s) shall make its filing in duplicate with the AAA, and simultaneously shall mail a copy of the Answer to the Claimant.

(iii) The Respondent(s):

- (1) May file a counterclaim with the AAA within ten (10) days after the letter from the AAA acknowledging receipt of the Demand. The filing shall be made in duplicate. The counterclaim shall set forth the nature of the claim, the amount in controversy, if any, and the remedy sought.
- (2) Simultaneously shall mail a copy of any counterclaim to the Claimant.
- (3) Shall include with its filing the applicable filing fee provided for by these rules.

(iv) The Claimant may file an Answer to the counterclaim with the AAA within ten (10) days after the date of the letter from the AAA acknowledging receipt of the counterclaim. The Answer shall provide Claimant's brief response to the counterclaim and the issues presented. The Claimant shall make its filing in duplicate with the AAA, and simultaneously shall mail a copy of the Answer to the Respondent(s).

c. The form of any filing in these rules shall not be subject to technical pleading requirements.

5. Changes of Claim

Before the appointment of the arbitrator, if either party desires to offer a new or different claim or counterclaim, such party must do so in writing by filing a written statement with the AAA and simultaneously mailing a copy to the other party(s), who shall have ten (10) days from the date of such mailing within which to file an answer with the AAA. After the appointment of the arbitrator, a party may offer a new or different claim or counterclaim only at the discretion of the arbitrator.

6. Administrative and Mediation Conferences

Before the appointment of the arbitrator, any party may request, or the AAA, in its discretion, may schedule an administrative conference with a representative of the AAA and the parties and/or their representatives. The purpose of the administrative conference is to organize and expedite the arbitration, explore its administrative aspects, establish the most efficient means of selecting an arbitrator, and to consider mediation as a dispute resolution option. There is no administrative fee for this service.

At any time after the filing of the Demand, with the consent of the parties, the AAA will arrange a mediation conference under its Mediation Rules to facilitate settlement. The mediator shall not be any arbitrator appointed to the case, except by mutual agreement of the parties. There is no administrative fee for initiating a mediation under AAA Mediation Rules for parties to a pending arbitration.

7. Discovery

The arbitrator shall have the authority to order such discovery, by way of deposition, interrogatory, document

production, or otherwise, as the arbitrator considers necessary to a full and fair exploration of the issues in dispute, consistent with the expedited nature of arbitration.

8. Arbitration Management Conference

As soon as possible after the appointment of the arbitrator but not later than sixty (60) days thereafter, the arbitrator shall conduct an Arbitration Management Conference with the parties and/or their representatives, in person or by telephone, to explore and resolve matters that will expedite the arbitration proceedings. The specific matters to be addressed include:

- (i) the issues to be arbitrated;
- (ii) the date, time, place and estimated duration of the hearing;
- (iii) the resolution of outstanding discovery issues and establishment of discovery parameters;
- (iv) the law, standards, rules of evidence and burdens of proof that are to apply to the proceeding;
- (v) the exchange of stipulations and declarations regarding facts, exhibits, witnesses and other issues;
- (vi) the names of witnesses (including expert witnesses), the scope of witness testimony, and witness exclusion;
- (vii) the value of bifurcating the arbitration into a liability phase and damages phase;
- (viii) the need for a stenographic record;
- (ix) whether the parties will summarize their arguments orally or in writing;
- (x) the form of the award;
- (xi) any other issues relating to the subject or conduct of the arbitration;
- (xii) the allocation of attorney's fees and costs.

The arbitrator shall issue oral or written orders reflecting his or her decisions on the above matters and may conduct additional conferences when the need arises.

There is no AAA administrative fee for an Arbitration Management Conference.

9. Location of the Arbitration

The parties may designate the location of the arbitration by mutual agreement. In the absence of such agreement before the appointment of the arbitrator, any party may request a specific hearing location by notifying the AAA in writing and simultaneously mailing a copy of the request to the other party(s). If the AAA receives no objection within ten (10) days of the date of the request, the hearing shall be held at the requested location. If a timely objection is filed with the AAA, the AAA shall have the power to determine the location and its decision shall be final and binding. After the appointment of the arbitrator, the arbitrator shall resolve all disputes regarding the location of the hearing.

10. Date and Time of Hearing

The arbitrator shall have the authority to set the date and time of the hearing in consultation with the parties.

11. Qualifications to Serve as Arbitrator and Rights of Parties to Disqualify Arbitrator

- a. Standards of Experience and Neutrality
 - (i) Arbitrators serving under these rules shall be experienced in the field of employment law.

- (ii) Arbitrators serving under these rules shall have no personal or financial interest in the results of the proceedings in which they are appointed and shall have no relation to the underlying dispute or to the parties or their counsel that may create an appearance of bias.
- (iii) The roster of available arbitrators will be established on a non-discriminatory basis, diverse by gender, ethnicity, background and qualifications.
- (iv) The Association may, upon request of a party or upon its own initiative, supplement the list of proposed arbitrators in disputes arising out of individually negotiated employment contracts with persons from the regular Commercial Roster, to allow the Association to respond to the particular needs of the dispute. In multi-arbitrator disputes, at least one of the arbitrators shall be experienced in the field of employment law.

b. Standards of Disclosure by Arbitrator

Prior to accepting appointment, the prospective arbitrator shall disclose all information that might be relevant to the standards of neutrality set forth in this Section, including but not limited to service as a neutral in any past or pending case involving any of the parties and/or their representatives or that may prevent a prompt hearing.

c. Disqualification for Failure To Meet Standards of Experience and Neutrality

An arbitrator may be disqualified in two ways:

- (i) No later than ten (10) days after the appointment of the arbitrator, all parties jointly may challenge the qualifications of an arbitrator by communicating their objection to the AAA in writing. Upon receipt of a joint objection, the arbitrator shall be replaced.
- (ii) Any party may challenge the qualifications of an arbitrator by communicating its objection to the AAA in writing. Upon receipt of the objection, the AAA either shall replace the arbitrator or communicate the objection to the other parties. If any party believes that the objection does not merit disqualification of the arbitrator, the party shall so communicate to the AAA and to the other parties within ten (10) days of the receipt of the objection from the AAA. Upon objection of a party to the service of an arbitrator, the AAA shall determine whether the arbitrator should be disqualified and shall inform the parties of its decision, which shall be conclusive.

12. Number and Appointment of Neutral Arbitrators

- a. If the parties do not specify the number of arbitrators, the dispute shall be heard and determined by one arbitrator. If the parties cannot agree upon the number of arbitrators, the AAA shall have the authority to determine the number of arbitrators.
- b. If the parties have not appointed an arbitrator and have not provided any method of appointment, the arbitrator shall be appointed in the following manner:
 - (i) Immediately after it receives the Demand, the AAA shall mail simultaneously to each party a letter containing an identical list of the names of all arbitrators who are members of the regional Employment Dispute Resolution Roster.
 - (ii) Each party shall have ten (10) days from the date of the letter in which to select the name of a mutually acceptable arbitrator to hear and determine their dispute. If the parties cannot agree upon a mutually acceptable arbitrator, they shall so notify the AAA. Within ten (10) days of the receipt of that notice, the AAA shall send the parties a shorter list of arbitrators who are members of the regional Employment Dispute Resolution Roster. Each party shall have ten (10) days from the date of the letter containing the revised list to strike any names objected to, number the remaining names in order of preference, and return the list to the AAA. If a party does not return the list within the time specified, all of the listed persons shall be deemed acceptable to that party.
 - (iii) The AAA shall invite the acceptance of the arbitrator whom both parties have selected as mutually acceptable or, in the case of resort to the ranking procedure, the arbitrator who has received the highest rating in the order of preference that the parties have specified.
 - (iv) If the parties fail to agree on any of the persons whom the AAA submits for consideration, or if mutually acceptable arbitrators are unable to act, or if for any other reason the appointment cannot be made from the list of persons whom the AAA submits for consideration, the AAA shall have the power to make the appointment from among other members of the Roster without the submission of additional lists.

13. Vacancies

If for any reason an arbitrator is unable to perform the duties of the office, the AAA may, on proof satisfactory to it, declare the office vacant. The vacancy shall be filled in accordance with applicable provisions of these Rules.

In the event of a vacancy in a panel of neutral arbitrators after the hearings have commenced, the remaining arbitrator or arbitrators may continue with the hearing and determination of the controversy, unless the parties agree otherwise.

14. Representation

Any party may be represented by counsel or other authorized representative. For parties without representation the AAA will, upon request, provide reference to institutions which might offer assistance. A party who intends to be represented shall notify the other party and the AAA of the name and address of the representative at least ten (10) days prior to the date set for the hearing or conference at which that person is first to appear. If a representative files a Demand or an Answer, the obligation to give notice of representative status is deemed satisfied.

15. Stenographic Record

Any party desiring a stenographic record shall make arrangements directly with a stenographer and shall notify the other parties of these arrangements at least three days in advance of the hearing. The requesting party or parties shall pay the cost of the record. If the transcript is agreed by the parties, or determined by the arbitrator to be the official record of the proceeding, it must be provided to the arbitrator and made available to the other parties for inspection, at a date, time, and place determined by the arbitrator.

16. Interpreters

Any party wishing an interpreter shall make all arrangements directly with the interpreter and shall assume the costs of the service.

17. Attendance at Hearings

The arbitrator shall have the authority to exclude witnesses, other than a party, from the hearing during the testimony of any other witness. The arbitrator also shall have the authority to decide whether any person who is not a witness may attend the hearing.

18. Confidentiality

The arbitrator shall maintain the confidentiality of the arbitration and shall have the authority to make appropriate rulings to safeguard that confidentiality, unless the parties agree otherwise or the law provides to the contrary.

19. Postponements

The arbitrator: (1) may postpone any hearing upon the request of a party for good cause shown; (2) must postpone any hearing upon the mutual agreement of the parties; and (3) may postpone any hearing on his or her own initiative.

20. Oaths

Before proceeding with the first hearing, each arbitrator may take an oath of office and, if required by law, shall do so. The arbitrator may require witnesses to testify under oath administered by any duly qualified person and, if it is required by law or requested by any party, shall do so.

21. Majority Decision

All decisions and awards of the arbitrators must be by a majority, unless the unanimous decision of all arbitrators is expressly required by the arbitration agreement or by law.

22. Order of Proceedings and Communication with Arbitrators

A hearing shall be opened by: (1) filing the oath of the arbitrator, where required; (2) recording the date, time,

and place of the hearing; (3) recording the presence of the arbitrator, the parties, and their representatives, if any; and (4) receiving into the record the Demand and the Answer, if any. The arbitrator may, at the beginning of the hearing, ask for statements clarifying the issues involved.

The parties shall bear the same burdens of proof and burdens of producing evidence as would apply if their claims and counterclaims had been brought in court.

Witnesses for each party shall submit to direct and cross examination as approved by the arbitrator.

With the exception of the rules regarding the allocation of the burdens of proof and going forward with the evidence, the arbitrator has the authority to set the rules for the conduct of the proceedings and shall exercise that authority to afford a full and equal opportunity to all parties to present any evidence that the arbitrator deems material and relevant to the resolution of the dispute.

Documentary and other forms of physical evidence, when offered by either party, may be received in evidence by the arbitrator.

The names and addresses of all witnesses and a description of the exhibits in the order received shall be made a part of the record.

There shall be no ex parte communication with the arbitrator, unless the parties and the arbitrator agree to the contrary in advance of the communication.

23. Arbitration in the Absence of a Party or Representative

Unless the law provides to the contrary, the arbitration may proceed in the absence of any party or representative who, after due notice, fails to be present or fails to obtain a postponement. An award shall not be based solely on the default of a party. The arbitrator shall require the party who is in attendance to present such evidence as the arbitrator may require for the making of the award.

24. Evidence

The parties may offer such evidence as is relevant and material to the dispute and shall produce such evidence as the arbitrator deems necessary to an understanding and determination of the dispute. An arbitrator or other person authorized by law to subpoena witnesses or documents may do so upon the request of any party or independently.

The arbitrator shall be the judge of the relevance and materiality of the evidence offered, and conformity to legal rules of evidence shall not be necessary. The arbitrator may in his or her discretion direct the order of proof, bifurcate proceedings, exclude cumulative or irrelevant testimony or other evidence, and direct the parties to focus their presentations on issues the decision of which could dispose of all or part of the case. All evidence shall be taken in the presence of all of the arbitrators and all of the parties, except where any party is absent, in default, or has waived the right to be present.

25. Evidence by Affidavit or Declaration and Post-Hearing Filing of Documents or Other Evidence

The arbitrator may receive and consider the evidence of witnesses by affidavit, but shall give it only such weight as the arbitrator deems it entitled to after consideration of any objection made to its admission.

If the parties agree or the arbitrator directs that documents or other evidence may be submitted to the arbitrator after the hearing, the documents or other evidence shall be filed with the AAA for transmission to the arbitrator, unless the parties agree to a different method of distribution. All parties shall be afforded an opportunity to examine such documents or other evidence and to lodge appropriate objections, if any.

26. Inspection or Investigation

An arbitrator finding it necessary to make an inspection or investigation in connection with the arbitration shall direct the AAA to so advise the parties. The arbitrator shall set the date and time, and the AAA shall notify the parties. Any party who so desires may be present during the inspection or investigation. In the event that one or all parties are not present during the inspection or investigation, the arbitrator shall make an oral or written report to the parties and afford them an opportunity to comment.

27. Interim Measures

At the request of any party, the arbitrator may take whatever interim measures he or she deems necessary

with respect to the dispute, including measures for the conservation of property.

Such interim measures may be taken in the form of an interim award and the arbitrator may require security for the costs of such measures.

28. Closing of Hearing

The arbitrator shall specifically inquire of all parties whether they have any further proofs to offer or witnesses to be heard. Upon receiving negative replies or if satisfied that the record is complete, the arbitrator shall declare the hearing closed.

If briefs are to be filed, the hearing shall be declared closed as of the final date set by the arbitrator for the receipt of briefs. If documents are to be filed as provided in Section 25 and the date set for their receipt is later than that set for the receipt of briefs, the later date shall be the date of closing the hearing. The time limit within which the arbitrator is required to make the award shall commence to run, in the absence of other agreements by the parties, upon closing of the hearing.

29. Reopening of Hearing

The hearing may be reopened by the arbitrator upon the arbitrator's initiative, or upon application of a party for cause shown, at any time before the award is made. If reopening the hearing would prevent the making of the award within the specific time agreed on by the parties in the contract(s) out of which the controversy has arisen, the matter may not be reopened unless the parties agree on an extension of time. When no specific date is fixed in the contract, the arbitrator may reopen the hearing and shall have thirty (30) days from the closing of the reopened hearing within which to make an award.

30. Waiver of Oral Hearing

The parties may provide, by written agreement, for the waiver of oral hearings in any case. If the parties are unable to agree as to the procedure, the AAA shall specify a fair and equitable procedure.

31. Waiver of Objection/Lack of Compliance with These Rules

Any party who proceeds with the arbitration after knowledge that any provision or requirement of these rules has not been complied with, and who fails to state objections thereto in writing, shall be deemed to have waived the right to object.

32. Extensions of Time

The parties may modify any period of time by mutual agreement. The AAA or the arbitrator may for good cause extend any period of time established by these Rules, except the time for making the award. The AAA shall notify the parties of any extension.

33. Serving of Notice

Each party shall be deemed to have consented that any papers, notices, or process necessary or proper for the initiation or continuation of an arbitration under these Rules; for any court actions in connection therewith; or for the entry of judgment on an award made under these procedures may be served on a party by mail addressed to the party or its representative at the last known address or by personal service, in or outside the state where the arbitration is to be held.

The AAA and the parties may also use facsimile transmission, telex, telegram, or other written forms of electronic communication to give the notices required by these Rules.

34. The Award

a. The award shall be made promptly by the arbitrator and, unless otherwise agreed by the parties or specified by law, no later than thirty (30) days from the date of closing of the hearing or, if oral hearings have been waived, from the date of the AAA's transmittal of the final statements and proofs to the arbitrator.

b. An award issued under these rules shall be publicly available, on a cost basis. The names of the parties and witnesses will not be publicly available, unless a party expressly agrees to have its name made public in the award.

- c. The award shall be in writing and shall be signed by a majority of the arbitrators and shall provide the written reasons for the award unless the parties agree otherwise. It shall be executed in the manner required by law.
- d. The arbitrator may grant any remedy or relief that the arbitrator deems just and equitable, including any remedy or relief that would have been available to the parties had the matter been heard in court. The arbitrator shall, in the award, assess arbitration fees, expenses, and compensation as provided in Sections 38, 39, and 40 in favor of any party and, in the event any administrative fees or expenses are due the AAA, in favor of the AAA.
- e. The arbitrator shall have the authority to provide for the reimbursement of representative's fees, in whole or in part, as part of the remedy, in accordance with applicable law.
- f. If the parties settle their dispute during the course of the arbitration, the arbitrator may set forth the terms of the settlement in a consent award.
- g. The parties shall accept as legal delivery of the award the placing of the award or a true copy thereof in the mail, addressed to a party or its representative at the last known address, personal service of the award, or the filing of the award in any manner that may be required by law.
- h. The arbitrator's award shall be final and binding. Judicial review shall be limited, as provided by law.

35. Modification of Award

Within twenty (20) days after the transmittal of an award, any party, upon notice to the other parties, may request the arbitrator to correct any clerical, typographical, technical or computational errors in the award. The arbitrator is not empowered to redetermine the merits of any claim already decided.

The other parties shall be given ten (10) days to respond to the request. The arbitrator shall dispose of the request within twenty (20) days after transmittal by the AAA to the arbitrator of the request and any response thereto.

If applicable law requires a different procedural time frame, that procedure shall be followed.

36. Release of Documents for Judicial Proceedings

The AAA shall, upon the written request of a party, furnish to the party, at that party's expense, certified copies of any papers in the AAA's case file that may be required in judicial proceedings relating to the arbitration.

37. Judicial Proceedings and Exclusion of Liability

- a. No judicial proceeding by a party relating to the subject matter of the arbitration shall be deemed a waiver of the party's right to arbitrate.
- b. Neither the AAA nor any arbitrator in a proceeding under these rules is or shall be considered a necessary or proper party in judicial proceedings relating to the arbitration.
- c. Parties to these procedures shall be deemed to have consented that judgment upon the arbitration award may be entered in any federal or state court having jurisdiction.
- d. Neither the AAA nor any arbitrator shall be liable to any party for any act or omission in connection with any arbitration conducted under these procedures.

38. Administrative Fees

As a not-for-profit organization, the AAA shall prescribe filing and other administrative fees to compensate it for the cost of providing administrative services. The AAA administrative fee schedule in effect at the time the demand for arbitration or submission agreement is received shall be applicable.

The filing fee shall be advanced by the initiating party or parties, subject to final apportionment by the arbitrator in the award.

The AAA may, in the event of extreme hardship on any party, defer or reduce the administrative fees.

39. Expenses

Unless otherwise agreed by the parties, the expenses of witnesses for either side shall be borne by the party producing such witnesses. All expenses of the arbitration, including required travel and other expenses of the arbitrator, AAA representatives, and any witness and the costs relating to any proof produced at the direction of the arbitrator, shall be borne equally by the parties, unless they agree otherwise or unless the arbitrator directs otherwise in the award.

The arbitrator's compensation shall be borne equally by the parties unless they agree otherwise, or unless the law provides otherwise.

40. Neutral Arbitrator's Compensation

Arbitrators shall charge a rate consistent with the arbitrator's stated rate of compensation. If there is disagreement concerning the terms of compensation, an appropriate rate shall be established with the arbitrator by the AAA and confirmed to the parties.

Any arrangement for the compensation of a neutral arbitrator shall be made through the AAA and not directly between the parties and the arbitrator. Payment of the arbitrator's fees and expenses shall be made by the AAA from the fees and moneys collected by the AAA from the parties for this purpose.

41. Deposits

The AAA may require the parties to deposit in advance of any hearings such sums of money as it deems necessary to cover the expenses of the arbitration, including the arbitrator's fee, if any, and shall render an accounting to the parties and return any unexpended balance at the conclusion of the case.

42. Interpretation and Application of Rules

The arbitrator shall interpret and apply these rules as they relate to the arbitrator's powers and duties. When there is more than one arbitrator and a difference arises among them concerning the meaning or application of these Rules, it shall be resolved by a majority vote. If that is not possible, either an arbitrator or a party may refer the question to the AAA for final decision. All other procedures shall be interpreted and applied by the AAA.

For disputes arising out of employer-promulgated plans:

ADMINISTRATIVE FEE SCHEDULE

Administrative Fee

The AAA's administrative fees are based on filing and service charges. Arbitrator compensation is not included in this schedule. Unless the parties agree otherwise, arbitrator compensation and administrative fees are subject to allocation by the arbitrator in the award.

Filing Fees

In cases before a single arbitrator, a nonrefundable filing fee in the amount of \$500 is payable in full by a filing party when a claim is filed, unless the plan provides otherwise.

In cases before three or more arbitrators, a nonrefundable filing fee in the amount of \$1,500 is payable in full by a filing party when a claim is filed, unless the plan provides otherwise.

Hearing Fees

For each day of hearing held before a single arbitrator, an administrative fee of \$150 is payable by each party.

For each day of hearing held before a multi-arbitrator panel, an administrative fee of \$250 is payable by each party.

There is no AAA hearing fee for the initial Arbitration Management Conference.

Postponement/Cancellation Fees

A fee of \$150 is payable by a party causing a postponement of any hearing scheduled before a single arbitrator.

A fee of \$250 is payable by a party causing a postponement of any hearing scheduled before a multi-arbitrator panel.

Hearing Room Rental

The hearing fees described above do not cover the rental of hearing rooms, which are available on a rental basis. Check with the administrator for availability and rates.

Suspension for Nonpayment

If arbitrator compensation or administrative charges have not been paid in full, the administrator may so inform the parties in order that one of them may advance the required payment. If such payments are not made, the arbitrator may order the suspension or termination of the proceedings. If no arbitrator has yet been appointed, the administrator may suspend the proceedings.

For disputes arising out of individually-negotiated employment agreements and contracts and commission sales agreements

The AAA's Commercial Fee Schedule, listed below, will apply to disputes arising out of individually-negotiated employment agreements and contracts and commission sales agreements. Any questions or disagreements about whether a matter arises out of an employer-promulgated plan or an individually-negotiated agreement or contract shall be determined by the AAA and its determination shall be final.

Administrative Fee

The administrative fees of the AAA are based on the amount of the claim or counterclaim. Arbitrator compensation is not included in this schedule. Unless the parties agree otherwise, arbitrator compensation and administrative fees are subject to allocation by the arbitrator in the award.

Fees

A nonrefundable initial filing fee is payable in full by a filing party when a claim, counterclaim or additional claim is filed.

A case service fee will be incurred for all cases that proceed to their first hearing. This fee will be payable in advance at the time that the first hearing is scheduled. This fee will be refunded at the conclusion of the case if no hearings have occurred.

However, if the Association is not notified at least 24 hours before the time of the scheduled hearing, the case service fee will remain due and will not be refunded.

These fees will be billed in accordance with the following schedule:

Amount of Claim	Initial Filing Fee	Case Service Fee
Above \$0 to \$10,000	\$500	N/A
Above \$10,000 to \$75,000	\$750	N/A
Above \$75,000 to \$150,000	\$1,250	\$750
Above \$150,000 to \$300,000	\$2,750	\$1,000
Above \$300,000 to \$500,000	\$4,250	\$1,250
Above \$500,000 to \$1,000,000	\$6,000	\$2,000
Above \$1,000,000 to \$7,000,000	\$8,500	\$2,500
Above \$7,000,000 to \$10,000,000	\$13,000	\$3,000
Above \$10,000,000	*	*
No Amount Stated	\$3,250	\$750

*Contact your local AAA office for fees for claims in excess of \$10 million.

** This fee is applicable when no amount can be stated at the time of filing, or when a claim or counterclaim is not for a monetary amount. The fees are subject to increase or decrease when the claim or counterclaim is disclosed.

The minimum fees for any case having three or more arbitrators are \$2,750 for the filing fee, plus a \$1,000 case service fee.

Hearing Room Rental

The fees described above do not cover the rental of hearing rooms, which are available on a rental basis. Check with the AAA for availability and rates.

EMPLOYMENT MEDIATION RULES

1. Agreement of Parties

Whenever, by provision in an employment dispute resolution program, or by separate submission, the parties have provided for mediation or conciliation of existing or future disputes under the auspices of the American Arbitration Association (hereinafter "AAA") or under these rules, they shall be deemed to have made these rules, as amended and in effect as of the date of the submission of the dispute, a part of their agreement.

2. Initiation of Mediation

Any party to an employment dispute may initiate mediation by filing with the AAA a submission to mediation or a written request for mediation pursuant to these rules, together with the applicable administrative fee.

3. Request for Mediation

A request for mediation shall contain a brief statement of the nature of the dispute and the names, addresses, and telephone numbers of all parties to the dispute and those who will represent them, if any, in the mediation. The initiating party shall simultaneously file two copies of the request with the AAA and one copy with every other party to the dispute.

4. Appointment of Mediator

Upon receipt of a request for mediation, the AAA will appoint a qualified mediator to serve. Normally, a single mediator will be appointed unless the parties agree otherwise or the AAA determines otherwise. If the agreement of the parties names a mediator or specifies a method of appointing a mediator, that designation or method shall be followed.

5. Qualifications of Mediator

No person shall serve as a mediator in any dispute in which that person has any financial or personal interest in the result of the mediation, except by the written consent of all parties. Prior to accepting an appointment, the prospective mediator shall disclose any circumstance likely to create a presumption of bias or prevent a prompt meeting with the parties. Upon receipt of such information, the AAA shall either replace the mediator or immediately communicate the information to the parties for their comments. In the event that the parties disagree as to whether the mediator shall serve, the AAA will appoint another mediator. The AAA is authorized to appoint another mediator if the appointed mediator is unable to serve promptly.

6. Vacancies

If any mediator shall become unwilling or unable to serve, the AAA will appoint another mediator, unless the parties agree otherwise.

7. Representation

Any party may be represented by a person of the party's choice. The names and addresses of such persons shall be communicated in writing to all parties and to the AAA.

8. Date, Time, and Place of Mediation

The mediator shall fix the date and the time of each mediation session. The mediation shall be held at the appropriate regional office of the AAA, or at any other convenient location agreeable to the mediator and the

parties, as the mediator shall determine.

9. Identification of Matters in Dispute

At least ten (10) days prior to the first scheduled mediation session, each party shall provide the mediator with a brief memorandum setting forth its position with regard to the issues that need to be resolved. At the discretion of the mediator, such memoranda may be mutually exchanged by the parties.

At the first session, the parties will be expected to produce all information reasonably required for the mediator to understand the issues presented. The mediator may require any party to supplement such information.

10. Authority of Mediator

The mediator does not have the authority to impose a settlement on the parties but will attempt to help them reach a satisfactory resolution of their dispute. The mediator is authorized to conduct joint and separate meetings with the parties and to make oral and written recommendations for settlement. Whenever necessary, the mediator may also obtain expert advice concerning technical aspects of the dispute, provided that the parties agree and assume the expenses of obtaining such advice. Arrangements for obtaining such advice shall be made by the mediator or the parties, as the mediator shall determine.

The mediator is authorized to end the mediation whenever, in the judgment of the mediator, further efforts at mediation would not contribute to a resolution of the dispute between the parties.

11. Privacy

Mediation sessions are private. The parties and their representatives may attend mediation sessions. Other persons may attend only with the permission of the parties and with the consent of the mediator.

12. Confidentiality

Confidential information disclosed to a mediator by the parties or by witnesses in the course of the mediation shall not be divulged by the mediator. All records, reports, or other documents received by a mediator while serving in that capacity shall be confidential. The mediator shall not be compelled to divulge such records or to testify in regard to the mediation in any adversary proceeding or judicial forum.

The parties shall maintain the confidentiality of the mediation and shall not rely on, or introduce as evidence in any arbitral, judicial, or other proceeding:

- a. views expressed or suggestions made by another party with respect to a possible settlement of the dispute;
- b. admissions made by another party in the course of the mediation proceedings;
- c. proposals made or views expressed by the mediator; or
- d. the fact that another party had or had not indicated willingness to accept a proposal for settlement made by the mediator.

13. No Stenographic Record

There shall be no stenographic record of the mediation process.

14. Termination of Mediation

The mediation shall be terminated:

- a. by the execution of a settlement agreement by the parties;
- b. by a written declaration of the mediator to the effect that further efforts at mediation are no longer worthwhile; or

c. by a written declaration of a party or parties to the effect that the mediation proceedings are terminated.

15. Exclusion of Liability

Neither the AAA nor any mediator is a necessary party in judicial proceedings relating to the mediation.

Neither the AAA nor any mediator shall be liable to any party for any act or omission in connection with any mediation conducted under these rules.

16. Interpretation and Application of Rules

The mediator shall interpret and apply these rules insofar as they relate to the mediator's duties and responsibilities. All other rules shall be interpreted and applied by the AAA.

17. Expenses

The expenses of witnesses for either side shall be paid by the party producing such witnesses. All other expenses of the mediation, including required traveling and other expenses of the mediator and representatives of the AAA, and the expenses of any witness and the cost of any proofs or expert advice produced at the direct request of the mediator, shall be borne equally by the parties unless they agree otherwise.

MEDIATION FEE SCHEDULE

Mediation fees vary around the country. Please check with the AAA regional office or case management center nearest to you for fee information and mediator availability.

Rules, forms, procedures and guides are subject to periodic change and updating. To ensure that you have the most current information, see our World Wide Web home page at www.adr.org

AAA121-1/01

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The U.S. Equal Employment Opportunity Commission

EEOC NOTICE

Number 915.002

Date July 10, 1997

1. SUBJECT: Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment
2. PURPOSE: This policy statement sets out the Commission's policy on the mandatory binding arbitration of employment discrimination disputes imposed as a condition of employment.
3. EFFECTIVE DATE: Upon issuance.
4. EXPIRATION DATE: As an exception to EEOC Order 205.001, Appendix B, Attachment 4, § a(5), this Notice will remain in effect until rescinded or superseded.
5. ORIGINATOR: Coordination and Guidance Programs, Office of Legal Counsel.
6. INSTRUCTIONS: File in Volume II of the EEOC Compliance Manual.
7. SUBJECT MATTER:

The United States Equal Employment Opportunity Commission (EEOC or Commission), the federal agency charged with the interpretation and enforcement of this nation's employment discrimination laws, has taken the position that agreements that mandate binding arbitration of discrimination claims as a condition of employment are contrary to the fundamental principles evinced in these laws. EEOC Motions on Alternative Dispute Resolution, Motion 4 (adopted Apr. 25, 1995), 80 Daily Lab. Rep. (BNA) E-1 (Apr. 26, 1995).¹ This policy statement sets out in further detail the basis for the Commission's position.

I. Background

An increasing number of employers are requiring as a condition of employment that applicants and employees give up their right to pursue employment discrimination claims in court and agree to resolve disputes through binding arbitration. These agreements may be presented in the form of an employment contract or be included in an employee handbook or elsewhere. Some employers have even included such agreements in employment applications. The use of these agreements is not limited

to particular industries, but can be found in various sectors of the workforce, including, for example, the securities industry, retail, restaurant and hotel chains, health care, broadcasting, and security services. Some individuals subject to mandatory

arbitration agreements have challenged the enforceability of these agreements by bringing employment discrimination actions in the courts. The Commission is not unmindful of the case law enforcing specific mandatory arbitration agreements, in particular, the Supreme Court's decision in *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 33 (1991).² Nonetheless, for the reasons stated herein, the Commission believes that such agreements are inconsistent with the civil rights laws.

II. The Federal Civil Rights Laws Are Squarely Based In This Nation's History And Constitutional Framework And Are Of A Singular National Importance

Federal civil rights laws, including the laws prohibiting discrimination in employment, play a unique role in American jurisprudence. They flow directly from core Constitutional principles, and this nation's history testifies to their necessity and profound importance. Any analysis of the mandatory arbitration of rights guaranteed by the employment discrimination laws must, at the outset, be squarely based in an understanding of the history and purpose of these laws.

Title VII of the historic Civil Rights Act of 1964, 42 U.S.C. § 2000e et seq., was enacted to ensure equal opportunity in employment, and to secure the fundamental right to equal protection guaranteed by the Fourteenth Amendment to the Constitution.³ Congress considered this national policy against discrimination to be of the "highest priority" (*Newman v. Piggie Park Enters.*, 390 U.S. 400, 402 (1968)), and of "paramount importance" (H.R. Rep. No. 88-914, pt. 2 (1963) (separate views of Rep. McCulloch et al.)),⁴ reprinted in 1964 Leg. Hist. at 2123.⁵ The Civil Rights Act of 1964, 42 U.S.C. § 2000a et seq., was intended to conform "[t]he practice of American democracy . . . to the spirit which motivated the Founding Fathers of this Nation -- the ideals of freedom, equality, justice, and opportunity." H.R. Rep. No. 88-914, pt. 2 (1963) (separate views of Rep. McCulloch et al.), reprinted in 1964 Leg. Hist. at 2123. President John F. Kennedy, in addressing the nation regarding his intention to introduce a comprehensive civil rights bill, stated the issue as follows:

We are confronted primarily with a moral issue. It is as old as the Scriptures and it is as clear as the American Constitution.

The heart of the question is whether all Americans are to be afforded equal rights and equal opportunities, whether we are going to treat our fellow Americans as we want to be treated.

President John F. Kennedy's Radio and Television Report to the American People on Civil Rights (June 11, 1963), Pub. Papers 468, 469 (1963).⁶

Title VII is but one of several federal employment discrimination laws enforced by the Commission which are "part of a wider statutory scheme to protect employees in the workplace nationwide," *McKennon v. Nashville Banner Publ'g Co.*, 513 U.S.

352, 357 (1995). See the Equal Pay Act of 1963 ("EPA"), 29 U.S.C. § 206(d); the Age Discrimination in Employment Act of 1967 ("ADEA"), 29 U.S.C. §§ 621 et seq.; and the Americans with Disabilities Act of 1990 ("ADA"), 42 U.S.C. §§ 12101 et seq. The ADEA was enacted "as part of an ongoing congressional effort to eradicate discrimination in the workplace" and "reflects a societal condemnation of invidious bias in employment decisions." McKennon, 513 U.S. at 357. The ADA explicitly provides that its purpose is, in part, to invoke congressional power to enforce the Fourteenth Amendment. 29 U.S.C. § 12101(b)(4). Upon signing the ADA, President George Bush remarked that "the American people have once again given clear expression to our most basic ideals of freedom and equality." President George Bush's Statement on Signing the Americans with Disabilities Act of 1990 (July 26, 1990), Pub. Papers 1070 (1990 Book II).

III. The Federal Government Has The Primary Responsibility For The Enforcement Of The Federal Employment Discrimination Laws

The federal employment discrimination laws implement national values of the utmost importance through the institution of public and uniform standards of equal opportunity in the workplace. See text and notes supra in Section II. Congress explicitly entrusted the primary responsibility for the interpretation, administration, and enforcement of these standards, and the public values they embody, to the federal government. It did so in three principal ways. First, it created the Commission, initially giving it authority to investigate and conciliate claims of discrimination and to interpret the law, see §§ 706(b) and 713 of Title VII, 42 U.S.C. §§ 2000e-5(b) and 2000e-12, and subsequently giving it litigation authority in order to bring cases in court that it could not administratively resolve, see § 706(f)(1) of Title VII, 42 U.S.C. § 2000e-5(f)(1). Second, Congress granted certain enforcement authority to the Department of Justice, principally with regard to the litigation of cases involving state and local governments. See §§ 706(f)(1) and 707 of Title VII, 42 U.S.C. §§ 2000e-5(f)(1) and 2000e-6. Third, it established a private right of action to enable aggrieved individuals to bring their claims directly in the federal courts, after first administratively bringing their claims to the Commission. See § 706(f)(1) of Title VII, 42 U.S.C. § 2000e-5(f)(1).⁷

While providing the states with an enforcement role, see 42 U.S.C. §§ 2000e-5(c) and (d), as well as recognizing the importance of voluntary compliance by employers, see 42 U.S.C. § 2000e-5(b), Congress emphasized that it is the federal government that has ultimate enforcement responsibility. As Senator Humphrey stated, "[t]he basic rights protected by [Title VII] are rights which accrue to citizens of the United States; the Federal Government has the clear obligation to see that these rights are fully protected." 110 Cong. Rec. 12725 (1964). Cf. *General Tel. Co. v. EEOC*, 446 U.S. 318, 326 (1980) (in bringing enforcement actions under Title VII, the EEOC "is guided by 'the overriding public interest in equal employment

opportunity . . . asserted through direct Federal enforcement'") (quoting 118 Cong. Rec. 4941 (1972)).

The importance of the federal government's role in the enforcement of the civil rights laws was reaffirmed by Congress in the ADA, which explicitly provides that its purposes include "ensur[ing] that the Federal Government plays a central role in enforcing the standards established in [the ADA] on behalf of individuals with disabilities." 42 U.S.C. § 12101(b)(3).

IV. Within This Framework, The Federal Courts Are Charged With The Ultimate Responsibility For Enforcing The Discrimination Laws

While the Commission is the primary federal agency responsible for enforcing the employment discrimination laws, the courts have been vested with the final responsibility for statutory enforcement through the construction and interpretation of the statutes, the adjudication of claims, and the issuance of relief.⁸ See, e.g., *Kremer v. Chemical Constr. Corp.*, 454 U.S. 461, 479 n.20 (1982) ("federal courts were entrusted with ultimate enforcement responsibility" of Title VII); *New York Gaslight Club, Inc. v. Carey*, 447 U.S. 54, 64 (1980) ("Of course the 'ultimate authority' to secure compliance with Title VII resides in the federal courts").⁹

A. The Courts Are Responsible For The Development And Interpretation Of The Law

As the Supreme Court emphasized in *Alexander v. Gardner-Denver Co.*, 415 U.S. 36, 57 (1974), "the resolution of statutory or constitutional issues is a primary responsibility of courts, and judicial construction has proved especially necessary with respect to Title VII, whose broad language frequently can be given meaning only by reference to public law concepts." This principle applies equally to the other employment discrimination statutes.

While the statutes set out the basic parameters of the law, many of the fundamental legal principles in discrimination jurisprudence have been developed through judicial interpretations and case law precedent. Absent the role of the courts, there might be no discrimination claims today based on, for example, the adverse impact of neutral practices not justified by business necessity, see *Griggs v. Duke Power Co.*, 401 U.S. 424 (1974), or sexual harassment, see *Harris v. Forklift Sys., Inc.*, 510 U.S. 17 (1993); *Meritor Savings Bank, FSB v. Vinson*, 477 U.S. 57 (1986). Yet these two doctrines have proved essential to the effort to free the workplace from unlawful discrimination, and are broadly accepted today as key elements of civil rights law.

B. The Public Nature Of The Judicial Process Enables The Public, Higher Courts, And Congress To Ensure That The Discrimination Laws Are Properly Interpreted And Applied

Through its public nature -- manifested through published decisions -- the exercise of judicial authority is subject to

public scrutiny and to system-wide checks and balances designed to ensure uniform expression of and adherence to statutory principles. When courts fail to interpret or apply the antidiscrimination laws in accord with the public values underlying them, they are subject to correction by higher level courts and by Congress.

These safeguards are not merely theoretical, but have enabled both the Supreme Court and Congress to play an active and continuing role in the development of employment discrimination law. Just a few of the more recent Supreme Court decisions overruling lower court errors include: *Robinson v. Shell Oil Co.*, 117 S. Ct. 843 (1997) (former employee may bring a claim for retaliation); *O'Connor v. Consolidated Coin Caterers, Corp.*, 116 S. Ct. 1307 (1996) (comparator in age discrimination case need not be under forty); *McKennon*, 513 U.S. 352 (employer may not use after-acquired evidence to justify discrimination); and *Harris* 510 U.S. 17 (no requirement that sexual harassment plaintiffs prove psychological injury to state a claim).

Congressional action to correct Supreme Court departures from congressional intent has included, for example, legislative amendments in response to Court rulings that: pregnancy discrimination is not necessarily discrimination based on sex (*General Elec. Co. v. Gilbert*, 429 U.S. 125 (1978), and *Nashville Gas Co. v. Satty*, 434 U.S. 136 (1977), overruled by Pregnancy Discrimination Act of 1978); that an employer does not have the burden of persuasion on the business necessity of an employment practice that has a disparate impact (*Wards Cove Packing Co. v. Atonio*, 490 U.S. 642 (1989), overruled by §§ 104 and 105 of the Civil Rights Act of 1991); that an employer avoids liability by showing that it would have taken the same action absent any discriminatory motive (*Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989), overruled, in part, by § 107 of the Civil Rights Act of 1991); that mandatory retirement pursuant to a benefit plan in effect prior to enactment of the ADEA is not prohibited age discrimination (*United Air Lines, Inc. v. McMann*, 434 U.S. 192 (1977), overruled by 1978 ADEA amendments); and, that age discrimination in fringe benefits is not unlawful (*Public Employees Retirement Sys. of Ohio v. Betts*, 492 U.S. 158 (1989), overruled by Older Workers Benefits Protection Act of 1990).

C. The Courts Play A Crucial Role In Preventing And Detering Discrimination And In Making Discrimination Victims Whole

The courts also play a critical role in preventing and deterring violations of the law, as well as providing remedies for discrimination victims. By establishing precedent, the courts give valuable guidance to persons and entities covered by the laws regarding their rights and responsibilities, enhancing voluntary compliance with the laws. By awarding damages, backpay, and injunctive relief as a matter of public record, the courts not only compensate victims of discrimination, but provide notice to the community, in a very tangible way, of the costs of discrimination. Finally, by issuing public decisions and orders,

the courts also provide notice of the identity of violators of the law and their conduct. As has been illustrated time and again, the risks of negative publicity and blemished business reputation can be powerful influences on behavior.

D. The Private Right Of Action With Its Guarantee Of Individual Access To The Courts Is Essential To The Statutory Enforcement Scheme

The private right of access to the judicial forum to adjudicate claims is an essential part of the statutory enforcement scheme. See, e.g., McKennon, 513 U.S. at 358 (granting a right of action to an injured employee is "a vital element" of Title VII, the ADEA, and the EPA). The courts cannot fulfill their enforcement role if individuals do not have access to the judicial forum. The Supreme Court has cautioned that, "courts should ever be mindful that Congress . . . thought it necessary to provide a judicial forum for the ultimate resolution of discriminatory employment claims. It is the duty of courts to assure the full availability of this forum." Gardner-Denver, 415 U.S. at 60 n.21.10

Under the enforcement scheme for the federal employment discrimination laws, individual litigants act as "private attorneys general." In bringing a claim in court, the civil rights plaintiff serves not only her or his private interests, but also serves as "the chosen instrument of Congress to vindicate 'a policy that Congress considered of the highest priority.'" Christiansburg Garment Co. v. EEOC, 434 U.S. 412, 418 (1978) (quoting Newman v. Piggie Park Enters., Inc., 390 U.S. 400, 402 (1968)). See also McKennon, 513 U.S. at 358 ("[t]he private litigant who seeks redress for his or her injuries vindicates both the deterrence and compensation objectives of the ADEA").

V. Mandatory Arbitration Of Employment Discrimination Disputes "Privatizes" Enforcement Of The Federal Employment Discrimination Laws, Thus Undermining Public Enforcement Of The Laws

The imposition of mandatory arbitration agreements as a condition of employment substitutes a private dispute resolution system for the public justice system intended by Congress to govern the enforcement of the employment discrimination laws. The private arbitral system differs in critical ways from the public judicial forum and, when imposed as a condition of employment, it is structurally biased against applicants and employees.

A. Mandatory Arbitration Has Limitations That Are Inherent And Therefore Cannot Be Cured By The Improvement Of Arbitration Systems

That arbitration is substantially different from litigation in the judicial forum is precisely the reason for its use as a form of ADR. Even the fairest of arbitral mechanisms will differ strikingly from the judicial forum.

1. The Arbitral Process Is Private In Nature And Thus Allows For Little Public Accountability

The nature of the arbitral process allows -- by design -- for minimal, if any, public accountability of arbitrators or arbitral decision-making. Unlike her or his counterparts in the judiciary, the arbitrator answers only to the private parties to the dispute, and not to the public at large. As the Supreme Court has explained:

A proper conception of the arbitrator's function is basic. He is not a public tribunal imposed upon the parties by superior authority which the parties are obliged to accept.

He has no general charter to administer justice for a community which transcends the parties. He is rather part of a system of self-government created by and confined to the parties. . . .

United Steelworkers of Am. v. Warrior and Gulf Navigation Co., 363 U.S. 574, 581 (1960) (quoting from Shulman, Reason, Contract, and Law in Labor Relations, 68 Harv. L. Rev. 999, 1016 (1955)).

The public plays no role in an arbitrator's selection; s/he is hired by the private parties to a dispute. Similarly, the arbitrator's authority is defined and conferred, not by public law, but by private agreement.¹¹ While the courts are charged with giving force to the public values reflected in the antidiscrimination laws, the arbitrator proceeds from a far narrower perspective: resolution of the immediate dispute. As noted by one commentator, "[a]djudication is more likely to do justice than . . . arbitration . . . precisely because it vests the power of the state in officials who act as trustees for the public, who are highly visible, and who are committed to reason." Owen Fiss, *Out of Eden*, 94 Yale L.J. 1669, 1673 (1985).

Moreover, because decisions are private, there is little, if any, public accountability even for employers who have been determined to have violated the law. The lack of public disclosure not only weakens deterrence (see discussion supra at 8), but also prevents assessment of whether practices of individual employers or particular industries are in need of reform. "The disclosure through litigation of incidents or practices which violate national policies respecting nondiscrimination in the work force is itself important, for the occurrence of violations may disclose patterns of noncompliance resulting from a misappreciation of [Title VII's] operation or entrenched resistance to its commands, either of which can be of industry-wide significance." McKennon, 513 U.S. at 358-59.

2. Arbitration, By Its Nature, Does Not Allow For The Development Of The Law

Arbitral decisions may not be required to be written or reasoned, and are not made public without the consent of the parties. Judicial review of arbitral decisions is limited to the narrowest of grounds.¹² As a result, arbitration affords no opportunity to build a jurisprudence through precedent.¹³

Moreover, there is virtually no opportunity for meaningful scrutiny of arbitral decision-making. This leaves higher courts and Congress unable to act to correct errors in statutory interpretation. The risks for the vigorous enforcement of the civil rights laws are profound. See discussion supra at section IV. B.

3. Additional Aspects Of Arbitration Systems Limit Claimants' Rights In Important Respects

Arbitration systems, regardless of how fair they may be, limit the rights of injured individuals in other important ways. To begin with, the civil rights litigant often has available the choice to have her or his case heard by a jury of peers, while in the arbitral forum juries are, by definition, unavailable. Discovery is significantly limited compared with that available in court and permitted under the Federal Rules of Civil Procedure. In addition, arbitration systems are not suitable for resolving class or pattern or practice claims of discrimination. They may, in fact, protect systemic discriminators by forcing claims to be adjudicated one at a time, in isolation, without reference to a broader -- and more accurate -- view of an employer's conduct.

B. Mandatory Arbitration Systems Include Structural Biases Against Discrimination Plaintiffs

In addition to the substantial and inevitable differences between the arbitral and judicial forums that have already been discussed, when arbitration of employment disputes is imposed as a condition of employment, bias inheres against the employee.¹⁴

First, the employer accrues a valuable structural advantage because it is a "repeat player." The employer is a party to arbitration in all disputes with its employees. In contrast, the employee is a "one-shot player"; s/he is a party to arbitration only in her or his own dispute with the employer. As a result, the employee is generally less able to make an informed selection of arbitrators than the employer, who can better keep track of an arbitrator's record. In addition, results cannot but be influenced by the fact that the employer, and not the employee, is a potential source of future business for the arbitrator.¹⁵ A recent study of nonunion employment law cases¹⁶ found that the more frequent a user of arbitration an employer is, the better the employer fares in arbitration.¹⁷

In addition, unlike voluntary post-dispute arbitration -- which must be fair enough to be attractive to the employee -- the employer imposing mandatory arbitration is free to manipulate the arbitral mechanism to its benefit. The terms of the private agreement defining the arbitrator's authority and the arbitral process are characteristically set by the more powerful party, the very party that the public law seeks to regulate. We are aware of no examples of employees who insist on the mandatory arbitration of future statutory employment disputes as a condition of accepting a job offer -- the very suggestion seems far-fetched. Rather, these agreements are imposed by employers

because they believe them to be in their interest, and they are made possible by the employer's superior bargaining power. It is thus not surprising that many employer-mandated arbitration systems fall far short of basic concepts of fairness. Indeed, the Commission has challenged -- by litigation, amicus curiae participation, or Commissioner charge -- particular mandatory arbitration agreements that include provisions flagrantly eviscerating core rights and remedies that are available under the civil rights laws.¹⁸

The Commission's conclusions in this regard are consistent with those of other analyses of mandatory arbitration. The Commission on the Future of Worker-Management Relations (the "Dunlop Commission") was appointed by the Secretary of Labor and the Secretary of Commerce to, in part, address alternative means to resolve workplace disputes. In its Report and Recommendations (Dec. 1994) ("Dunlop Report"), the Dunlop Commission found that recent employer experimentation with arbitration has produced a range of programs that include "mechanisms that appear to be of dubious merit for enforcing the public values embedded in our laws." Dunlop Report at 27. In addition, a report by the U.S. General Accounting Office, surveying private employers' use of ADR mechanisms, found that existing employer arbitration systems vary greatly and that "most" do not conform to standards recommended by the Dunlop Commission to ensure fairness. See "Employment Discrimination: Most Private-Sector Employers Use Alternative Dispute Resolution" at 15, HEHS-95-150 (July 1995).

The Dunlop Commission strongly recommended that binding arbitration agreements not be enforceable as a condition of employment:

The public rights embodied in state and federal employment law -- such as freedom from discrimination in the workplace . . . -- are an important part of the social and economic protections of the nation. Employees required to accept binding arbitration of such disputes would face what for many would be an inappropriate choice: give up your right to go to court, or give up your job.

Dunlop Report at 32. The Brock Commission (see supra n.13) agreed with the Dunlop Commission's opposition to mandatory arbitration of employment disputes and recommended that all employee agreements to arbitrate be voluntary and post-dispute. Brock Report at 81-82. In addition, the National Academy of Arbitrators recently issued a statement opposing mandatory arbitration as a condition of employment "when it requires waiver of direct access to either a judicial or administrative forum for the pursuit of statutory rights." See National Academy of Arbitrators' Statement and Guidelines (adopted May 21, 1997), 103 Daily Lab. Rep. (BNA) E-1 (May 29, 1997).

C. Mandatory Arbitration Agreements Will Adversely Affect The Commission's Ability To Enforce The Civil Rights Laws

The trend to impose mandatory arbitration agreements as a condition of employment also poses a significant threat to the EEOC's statutory responsibility to enforce the federal employment

discrimination laws. Effective enforcement by the Commission depends in large part on the initiative of individuals to report instances of discrimination to the Commission. Although employers may not lawfully deprive individuals of their statutory right to file employment discrimination charges with the EEOC or otherwise interfere with individuals' protected participation in investigations or proceedings under these laws,¹⁹ employees who are bound by mandatory arbitration agreements may be unaware that they nonetheless may file an EEOC charge. Moreover, individuals are likely to be discouraged from coming to the Commission when they know they will be unable to litigate their claims in court.²⁰ These chilling effects on charge filing undermine the Commission's enforcement efforts by decreasing channels of information, limiting the agency's awareness of potential violations of law, and impeding its ability to investigate possible unlawful actions and attempt informal resolution.

VI. Voluntary, Post-Dispute Agreements To Arbitrate Appropriately Balance The Legitimate Goals Of Alternate Dispute Resolution And The Need To Preserve The Enforcement Framework Of The Civil Rights Laws

The Commission is on record in strong support of voluntary alternative dispute resolution programs that resolve employment discrimination disputes in a fair and credible manner, and are entered into after a dispute has arisen. We reaffirm that support here. This position is based on the recognition that while even the best arbitral systems do not afford the benefits of the judicial system, well-designed ADR programs, including binding arbitration, can offer in particular cases other valuable benefits to civil rights claimants, such as relative savings in time and expense.²¹ Moreover, we recognize that the judicial system is not, itself, without drawbacks. Accordingly, an individual may decide in a particular case to forego the judicial forum and resolve the case through arbitration. This is consistent with civil rights enforcement as long as the individual's decision is freely made after a dispute has arisen.²²

VII. Conclusion

The use of unilaterally imposed agreements mandating binding arbitration of employment discrimination disputes as a condition of employment harms both the individual civil rights claimant and the public interest in eradicating discrimination. Those whom the law seeks to regulate should not be permitted to exempt themselves from federal enforcement of civil rights laws. Nor should they be permitted to deprive civil rights claimants of the choice to vindicate their statutory rights in the courts -- an avenue of redress determined by Congress to be essential to enforcement.

Processing Instructions For The Field And Headquarters

1. Charges should be taken and processed in conformity with priority charge processing procedures regardless of whether

the charging party has agreed to arbitrate employment disputes. Field offices are instructed to closely scrutinize each charge involving an arbitration agreement to determine whether the agreement was secured under coercive circumstances (e.g., as a condition of employment). The Commission will process a charge and bring suit, in appropriate cases, notwithstanding the charging party's agreement to arbitrate.

2. Pursuant to the statement of priorities in the National Enforcement Plan, see § B(1)(h), the Commission will continue to challenge the legality of specific agreements that mandate binding arbitration of employment discrimination disputes as a condition of employment. See, e.g., Briefs of the EEOC as Amicus Curiae in *Seus v. John Nuveen & Co.*, No. 96-CV-5971 (E.D. Pa.) (Br. filed Jan. 11, 1997); *Gibson v. Neighborhood Health Clinics, Inc.*, No. 96-2652 (7th Cir.) (Br. filed Sept. 23, 1996); *Johnson v. Hubbard Broadcasting, Inc.*, No. 4-96-107 (D. Minn.) (Br. Filed May 17, 1996); *Great Western Mortgage Corp. v. Peacock*, No. 96-5273 (3d Cir.) (Br. filed July 24, 1996).

/s/

Date

Gilbert F. Casellas
Chairman

1. Although binding arbitration does not, in and of itself, undermine the purposes of the laws enforced by the EEOC, the Commission believes that this is the result when it is imposed as a term or condition of employment.

2. The *Gilmer* decision is not dispositive of whether employment agreements that mandate binding arbitration of discrimination claims are enforceable. As explicitly noted by the Court, the arbitration agreement at issue in *Gilmer* was not contained in an employment contract. 500 U.S. at 25 n.2. Even if *Gilmer* had involved an agreement with an employer, the issue would remain open given the active role of the legislative branch in shaping the development of employment discrimination law. See discussion *infra* at section IV. B.

3. See, e.g., H.R. Rep. No. 88-914, pt. 1 (1963), reprinted in *United States Equal Employment Opportunity Commission, Legislative History of Title VII and XI of the Civil Rights Act of 1964* ("1964 Leg. Hist.") at 2016 (the Civil Rights Act of 1964 was "designed primarily to protect and provide more effective means to enforce. . . civil rights"); H.R. Rep. No. 88-914, pt. 2 (1963) (separate views of Rep. McCulloch et al.), reprinted in 1964 Leg. Hist. at 2122 ("[a] key purpose of the bill . . . is to secure to all Americans the equal protection of the laws of the United States and of the several States"); Charles & Barbara Whalen, *The Longest Debate: A legislative history of the 1964 Civil Rights Act* 104 (1985) (opening

statement of Rep. Celler on House debate of H.R. 7152: "The legislation before you seeks only to honor the constitutional guarantees of equality under the law for all. . . . [W]hat it does is to place into balance the scales of justice so that the living force of our Constitution shall apply to all people"; H.R. Rep. No. 92-238 (1971), reprinted in Senate Committee on Labor and Public Welfare, Subcommittee on Labor, Legislative History of the Equal Employment Opportunity Act of 1972 ("1972 Leg. Hist.") at 63 (1972 amendments to Title VII are a "reaffirmation of our national policy of equal opportunity in employment").

4. William McCulloch (R-Ohio) was the ranking Republican of Subcommittee No. 5 of the House Judiciary Committee, to which the civil rights bill (H.R. 7152) was referred for initial consideration by Congress. McCulloch was among the individuals responsible for working out a compromise bill that was ultimately substituted by the full Judiciary Committee for the bill reported out by Subcommittee No. 5. His views, which were joined by six members of Congress, are thus particularly noteworthy.

5. See also *Albemarle Paper Co. v. Moody*, 422 U.S. 405, 416 (1975) (The Civil Rights Act of 1964 is a "complex legislative design directed at an historic evil of national proportions").

6. Commitment to our national policy to eradicate discrimination continues today to be of the utmost importance. As President Clinton stated in his second inaugural address:

Our greatest responsibility is to embrace a new spirit of community for a new century The challenge of our past remains the challenge of our future: Will we be one Nation, one people, with one common destiny, or not? Will we all come together, or come apart?

The divide of race has been America's constant curse. And each new wave of immigrants gives new targets to old prejudices These forces have nearly destroyed our Nation in the past. They plague us still.

President William J. Clinton's Inaugural Address (Jan. 20, 1997), 33 Weekly Comp. Pres. Doc. 61 (Jan. 27, 1997).

7. Section 107 of the ADA specifically incorporates the powers, remedies, and procedures set forth in Title VII with respect to the Commission, the Attorney General, and aggrieved individuals. See 42 U.S.C. § 12117. Similar enforcement provisions are contained in the ADEA. See 29 U.S.C. §§ 626 and 628.

8. In addition, unlike arbitrators, courts have coercive authority, such as the contempt power, which they can use to secure compliance.

9. See also H.R. Rep. No. 88-914, pt.2 (1963) (separate views of Rep. McCulloch et al.), reprinted in 1964 Leg. Hist. at 2150 (explaining that EEOC was not given cease-and-desist powers

in the final House version of the Civil Rights Act of 1964, H.R. 7152, because it was "preferred that the ultimate determination of discrimination rest with the Federal judiciary").

10. See also 118 Cong. Rec. S7168 (March 6, 1972) (section-by-section analysis of H.R. 1746, the Equal Opportunity Act of 1972, as agreed to by the conference committees of each House; analysis of § 706(f)(1) provides that, while it is hoped that most cases will be handled through the EEOC with recourse to a private lawsuit as the exception, "as the individual's rights to redress are paramount under the provisions of Title VII it is necessary that all avenues be left open for quick and effective relief").

11. Article III of the Constitution provides federal judges with life tenure and salary protection to safeguard the independence of the judiciary. No such safeguards apply to the arbitrator. The importance of these safeguards was stressed in the debates on the 1972 amendments to Title VII. Senator Dominick, in offering an amendment giving the EEOC the right to file a civil action in lieu of cease-and-desist powers, explained that the purpose of the amendment was to "vest adjudicatory power where it belongs -- in impartial judges shielded from political winds by life tenure." 1972 Leg. Hist. at 549. The amendment was later revised in minor respects and adopted by the Senate.

12. Under the Federal Arbitration Act, arbitral awards may be vacated only for procedural impropriety such as corruption, fraud, or misconduct. 9 U.S.C. § 10. Judicially created standards of review allow an arbitral award to be vacated where it clearly violates a public policy that is explicit, well-defined, "dominant" and ascertainable from the law, see *United Paperworkers Int'l Union v. Misco, Inc.*, 484 U.S. 29, 43 (1987), or where it is in "manifest disregard" of the law, see *Wilko v. Swan*, 346 U.S. 427, 436-37 (1953). The latter standard of review has been described by one commentator as "a virtually insurmountable" hurdle. See Bret F. Randall, *The History, Application, and Policy of the Judicially Created Standards of Review for Arbitration Awards*, 1992 *BYU L. Rev.* 759, 767. But cf. *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1486-87 (1997) (in the context of mandatory employment arbitration of statutory disputes, the court interprets judicial review under the "manifest disregard" standard to be sufficiently broad to ensure that the law has been properly interpreted and applied).

13. Congress has recognized the inappropriateness of ADR where "a definitive or authoritative resolution of the matter is required for precedential value, and such a proceeding is not likely to be accepted generally as an authoritative precedent," see *Alternative Dispute Resolution Act*, 5 U.S.C. § 572(b)(1) (providing for use of ADR by federal administrative agencies where the parties agree); or where "the case involves complex or novel legal issues," see *Judicial Improvements and Access to Justice Act*, 28 U.S.C. § 652(c)(2) (providing for court-annexed arbitration; §§ 652(b)(1) and (2) also require the parties' consent to arbitrate constitutional or statutory civil rights claims). Similar findings were made by the U.S. Secretary of Labor's Task

Force on Excellence in State and Local Government Through Labor-Management Cooperation ("Brock Commission"), which was charged with examining labor-management cooperation in state and local government. The Task Force's report, "Working Together for Public Service" (1996) ("Brock Report"), recommended "Quality Standards and Key Principles for Effective Alternative Dispute Resolution Systems for Rights Guaranteed by Public Law and for Other Workplace Disputes" which include that "ADR should normally not be used in cases that represent tests of significant legal principles or class action." Brock Report at 82.

14. A survey of employment discrimination arbitration awards in the securities industry, which requires as a condition of employment that all brokers resolve employment disputes through arbitration, found that "employers stand a greater chance of success in arbitration than in court before a jury" and are subjected to "smaller" damage awards. See Stuart H. Bompey & Andrea H. Stempel, *Four Years Later: A Look at Compulsory Arbitration of Employment Discrimination Claims After Gilmer v. Interstate/Johnson Lane Corp.*, 21 *Empl. Rel. L.J.* 21, 43 (autumn 1995).

15. See, e.g., Julius G. Getman, *Labor Arbitration and Dispute Resolution*, 88 *Yale L.J.* 916, 936 (1979) ("an arbitrator could improve his chances of future selection by deciding favorably to institutional defendants: as a group, they are more likely to have knowledge about past decisions and more likely to be regularly involved in the selection process"); Reginald Alleyne, *Statutory Discrimination Claims: Rights 'Waived' and Lost in the Arbitration Forum*, 13 *Hofstra Lab. L.J.* 381, 428 (Spring 1996) ("statutory discrimination grievances relegated to . . . arbitration forums are virtually assured employer-favored outcomes," given "the manner of selecting, controlling, and compensating arbitrators, the privacy of the process and how it catalytically arouses an arbitrator's desire to be acceptable to one side").

16. Arbitration of labor disputes pursuant to a collective bargaining agreement is less likely to favor the employer as a repeat-player because the union, as collective bargaining representative, is also a repeat-player.

17. See Lisa Bingham, "Employment Arbitration: The effect of repeat-player status, employee category and gender on arbitration outcomes," (unpublished study on file with the author, an assistant professor at Indiana U. School of Public & Environmental Affairs).

18. Challenged agreements have included provisions that: (1) impose filing deadlines far shorter than those provided by statute; (2) limit remedies to "out-of-pocket" damages; (3) deny any award of attorney's fees to the civil rights claimant, should s/he prevail; (4) wholly deny or limit punitive and liquidated damages; (5) limit back pay to a time period much shorter than that provided by statute; (6) wholly deny or limit front pay to a time period far shorter than that ordered by courts; (7) deny any and all discovery; and (8) allow for payment by each party of one-half of the costs of arbitration and, should

the employer prevail, require the claimant, in the arbitrator's discretion, to pay the employer's share of arbitration costs as well.

19. See "Enforcement Guidance on non-waivable employee rights under Equal Employment Opportunity Commission (EEOC) statutes," Vol. III EEOC Compl. Man. (BNA) at N:2329 (Apr. 10, 1997).

20. The Commission remains able to bring suit despite the existence of a mandatory arbitration agreement because it acts "to vindicate the public interest in preventing employment discrimination," General Tel., 446 U.S. at 326. Cf. S.Rep. No. 101-263 (1990), reprinted in, Legislative History of The Older Workers Benefits Protection Act, at 354 (amendment to ADEA § 626(f)(4), which provides that "no waiver agreement may affect the Commission's rights and responsibilities to enforce [the ADEA]," was intended "as a clear statement of support for the principle that the elimination of age discrimination in the workplace is a matter of public as well as private interest"). As a practical matter, however, the Commission's ability to litigate is limited by its available resources.

21. Despite conventional wisdom to the contrary, the financial costs of arbitration can be significant and may represent no savings over litigation in a judicial forum. These costs may include the arbitrator's fee and expenses; fees charged by the entity providing arbitration services, which may include filing fees and daily administrative fees; space rental fees; and court reporter fees.

22. The Dunlop Commission similarly supported voluntary forms of ADR, but based its opposition to mandatory arbitration on the premise that the avenue of redress for statutory employment rights should be chosen by the individual rather than dictated by the employer. Dunlop Report at 33.

This page was last modified on July 6, 2000.

TO: Rochelle Kentov, Regional Director Region 12

*1 SUBJECT: Bentley's Luggage Corporation
Case 12-CA-16658
August 21, 1995

DIGEST NO.S:

506-6090-4900, 512-5006-5096, 512-5081-7000, 512-5090-7525, 596-0866-5000, 625- 2233-7200, 625-7728-2200

This case was submitted for advice on the following issues:

(1) whether the Employer violated Section 8(a)(1), (3) and (4) of the Act by requiring employees and applicants to sign an agreement requiring employees to submit their employment claims to binding arbitration and pay a portion of the costs before they seek redress from any other forum concerning employment issues or termination;

(2) whether the Employer unlawfully discharged the Charging Party because he refused to sign such an arbitration agreement;

FACTS

The Employer operates a chain of luggage stores nationwide. Its employees nationwide are not represented by any union. In November 1993, Charging Party Allen Robert Letwin (Letwin) began working for the Employer in its Ft. Lauderdale Galleria Mall store as a regular part-time sales employee.

On June 7, 1994, the Employer imposed a nationwide condition for continued employment, by requiring all current employees to sign an arbitration agreement which provided the following:

By remaining a Bentley's employee, you agree that before filing any legal action regarding your employment or the termination of your employment, the dispute will be submitted to binding arbitration before a neutral third party, pursuant to the procedures of the American Arbitration Association. You also agree that any lawsuit filed, before the arbitration has been conducted should be dismissed.... Each party will bear its own costs and attorneys' fees. The arbitrator's fee will be divided equally between the parties.

The Company emphasizes, and the employee hereby acknowledges, that employment with Bentley's is at-will and that neither this application nor any other document should be interpreted as creating a "just cause" standard of employment. The Company and the employee hereby agree that all claims, including claims alleging a contract, tort or violation of any statute, be submitted to arbitration. If a court decides that this policy is not enforceable for some claims, the employee and the Company agree that claims which are legally subject to this policy should be dismissed by the court.

The agreement appears to be in effect during employees' tenure with the Employer. Further, the agreement states several times that employment with the Employer is "at will" and termination need not be based on just cause.

Letwin was terminated on July 12, 1994, because he refused to sign the agreement. Prior to his termination, Letwin informed his supervisor, Store Manager Donna Pollio, that he felt that by signing he was giving up all his rights. Pollio agreed that she felt the agreement was "unfair" but insisted that it had to be signed in order for Letwin to keep his position. Letwin discussed his position regarding the arbitration agreement with fellow employees. They told Letwin that they too had problems with signing the agreement but that they could not afford to refuse to sign the agreements and lose their jobs.

*2 On October 11, Letwin filed the instant charge alleging that the Employer violated Section 8(a)(1) and (4) of the Act by terminating him because he refused to sign the arbitration agreement. On January 27, 1995, Letwin filed a first amended charge, which alleged that the Employer's conduct also violated Section 8(a)(3) and sought a remedy for all employees similarly situated to Letwin. [FN1]

On March 29, 1995, Letwin filed a second amended charge which alleged that the June 28, 1994, termination of William Kelly, another employee, for his refusal to sign the arbitration agreement also violated the Act.

The Employer has offered to settle this matter on the following terms: (1) the Employer will send a memorandum to all current employees stating that the arbitration agreement was not meant to prohibit employees from access to the Board; (2) the Employer will insert a clause in the arbitration agreement stating that it was not meant to prohibit employees from access to the Board; (3) the Employer will reinstate Letwin if he signs the modified arbitration agreement; (4) the Employer will pay backpay only for Letwin if he is reinstated; (5) a nonadmission clause.

ACTION

We conclude that the Region should issue a complaint, absent settlement, alleging that the Employer violated Section 8(a)(1) and (4) [FN2] of the Act by maintaining the arbitration agreement and discharging Letwin because he refused to sign the agreement.

Initially, we concluded that the Employer violated Section 8(a)(1) and (4) by maintaining the arbitration agreement and insisting that employees sign that agreement as a term and condition of employment. The agreement impermissibly requires employees to waive their statutory right to file charges with the Board.

Section 10(a) of the NLRA provides in relevant part that the Board is empowered ... to prevent any person from engaging in any unfair labor practice ... This power shall not be affected by any other means of adjustment or prevention that has been or may be established by agreement, law or otherwise. [FN3]

From its inception, the NLRA has permitted the Board to treat individual contracts of employment, when used to frustrate the exercise of statutory rights, as either void or voidable. In *National Licorice Co. v. NLRB*, [FN4] after the union obtained majority status, the employer refused to grant the union recognition and instead circulated a petition for a bargaining committee. The bargaining committee negotiated individual contracts between the employer and every employee, in which the employees relinquished the right to strike and the right to demand a union-security clause or a written contract with any union. While the contracts granted employees the right to arbitration as to wages and hours, they expressly foreclosed arbitration as to discharge. The Supreme Court found that the individual employment contract imposed illegal conditions on the exercise of Section 7 and 8 rights. The effect of the clause barring arbitration of discharge was to "discourage, if not forbid," the presentation of grievances, by discharged employees to the employer through a union, or in any way except personally. [FN5]

*3 Consistent with *National Licorice*, the Board has regularly held that an employer violates the Act when it insists that an employee waive his statutory right to file charges with the Board or to invoke his contractual grievance-arbitration procedure. [FN6] A union similarly violates Section 8(b)(1)(A) when it conditions use of the union's hiring hall on the signing of a form containing a waiver of an employee's right to sue the union because of an employment dispute. [FN7]

The arbitration agreement involved in this case has precisely the same unlawful effect as

these waiver demands or agreements long condemned by the Board. The arbitration agreement requires, as a condition of employment, that the employee subordinate his/her right to file charges with the Board concerning employment to the Employer's unilaterally chosen arbitration process. Hence, a Section 8(a)(4) and (1) complaint is warranted, absent settlement, as to the Employer's maintenance of the arbitration agreement as a term and condition of employment and its discharge of Letwin for refusing to sign the agreement.

We note that the complaint in *Kinder-Care*, supra, alleged only a Section 8(a)(1) violation, not an additional Section 8(a)(4) violation. However, the rule in *Kinder-Care*, which stated that employees had to bring their employment-related disputes to the employer "immediately," [FN8] did not explicitly bar employees from asserting their statutory rights, even though the Board construed the rule as having such an effect. On the other hand, in *Great Lakes Chemical Corp.*, supra, where employees were required to sign a statement waiving their rights to bring any legal action against the employer as a result of their layoff or termination, the Board affirmed the conclusion of the ALJ, at 622, that the employer violated Section 8(a)(4), as well as Section 8(a)(1), by conditioning employment on the signing of the waiver. Like the waiver demand in *Great Lakes Chemical*, supra, the arbitration agreement in this case explicitly requires an employee not to assert his statutory rights, and even to withdraw any legal actions instituted pursuant to those statutory rights, before using the Employer's compulsory arbitration procedure. The rule thus deters employees from seeking to file charges with the Board, because the rule requires those employees to resort to the Employer's arbitration procedure before filing charges or otherwise seeking to vindicate their employment rights. Such an open attack on an employee's right to seek access to the Board is appropriately litigated through a Section 8(a)(4) allegation. [FN9] Hence, a Section 8(a)(4) complaint is warranted even though Letwin was discharged for refusing to sign the arbitration agreement, not for filing a charge with the Board.

The Employer contends that this agreement is lawful under *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 111 S.Ct. 1647, 1655 (1991). In that case, Gilmer, a 62-year-old stockbroker employed by Interstate/Johnson Lane Corp., had been required as a condition of registration as a securities representative with the New York Stock Exchange to agree to arbitrate any dispute arising out of his employment or termination from employment. When Gilmer filed an ADEA charge with the EEOC following his termination, the employer sought to compel arbitration of the claim pursuant to the agreement. The Court held that the agreement was enforceable against Gilmer. Gilmer argued that the Federal Arbitration Act, 9 U.S.C. Sec. 1, (FAA) barred mandatory arbitration of "contracts of employment," because it stated that "nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." The Court held that it was "inappropriate" to discuss the scope of this exclusion because "the arbitration clause being enforced here is not contained in a contract of employment." [FN10] Instead, the arbitration agreement was part of Gilmer's registration with the New York Stock Exchange, and there was no claim or evidence that Gilmer and his employer were parties to an employment agreement that contained a written arbitration clause. Therefore, the Court specifically left "for another day" the meaning of Section 1 of the FAA. [FN11]

*4 The Court further noted that it found no evidence that Gilmer, an experienced businessman, "was coerced or defrauded into agreeing to the arbitration clause in his registration application." [FN12] The Court rejected the argument that there was inequality of bargaining power between Gilmer and his employer and noted that such mere inequality is not "a sufficient reason to hold that arbitration agreements are never enforceable in the employment context." [FN13] Instead, it held that such claims should be addressed in specific cases. [FN14] The Court also noted, at 1653, that an individual employee subject to an arbitration agreement could nonetheless file an ADEA charge with

the EEOC, as Gilmer had done. The Court further noted, *ibid.*, that the EEOC had the authority to investigate age discrimination problems even in the absence of a charge alleging a violation.

We conclude that Gilmer is not applicable in this case. In Gilmer, the Court stated that while not all statutory claims may not be appropriate for arbitration, the person entering into such an agreement must be held to the agreement, "unless Congress evidenced an intention to preclude a waiver of judicial remedies for the statutory rights at issue." [FN15] As noted above at page 4, Section 10(a) of the Act gives the Board authority to prevent or remedy unfair labor practices, regardless of any other dispute resolution mechanism that may be available. The Board's decision to defer to contractually-negotiated grievance-arbitration between an employer and a union is thus an exercise of the Board's discretionary authority and the antithesis of the purpose of the Employer's attempt here to preclude the Board from exercising its jurisdiction in any manner.

Moreover, the Court in Gilmer was merely enforcing an arbitration agreement that Gilmer had previously signed; it did not have to confront the question raised by this case, that is, whether the signing of an arbitration agreement that also constitutes a waiver of an employee's statutory rights is a lawful term and condition of employment. Thus, Gilmer does not overrule the Board's position, as set forth in the cases listed in fn. 8, *supra*, that efforts to secure such waivers from employees are unlawful. [FN16] We further note that while the EEOC can investigate age discrimination questions and problems on its own initiative, even in the absence of a charge, the Board requires the filing of a charge to initiate its processes; thus, any attempt by an employer to bar an employee from filing an unfair labor practice charge would foreclose the Board from exercising its statutory jurisdiction.

We further conclude that the Employer's arbitration plan is not comparable to or an adequate substitute for the Board's processes. The Act permits the employee to claim that his termination violated his statutory rights. The arbitration agreement, on the other hand, is essentially illusory because the Employer states that its employees are "at will" and no just cause is required to terminate an employee. [FN17] Thus, this agreement does not give an employee a basis upon which to claim that a termination is improper.

*5 The Employer also contends that the arbitration agreement does not bar the processing of an unfair labor practice charge. The clear language of the agreement is *contra*. Thus, the agreement specifically states that an asserted "violation of any statute" must be submitted to arbitration. Moreover, the Board affirmed an ALJ's rejection of a similar argument in *Construction and General Laborers, Local 304, supra*, at 607, noting that the fact that the agreement barred suits as to any matter meant that it was intended to bar unfair labor practice charges, even though the Board was not named in the agreement. Indeed, the Board has construed even vaguer language as requiring employees to waive their statutory rights to file charges. Thus, in *Kinder-Care Learning Centers, supra*, the employee handbook maintained a "parent communication rule" that stated that it was "essential" that employees bring their employment-related complaints to the employer "immediately" or use the company's problem-solving procedure; the penalty for failure to follow this procedure was discharge. The employer required employees to sign copies of this "parent communication rule," acknowledging that they had received a notice of the rule. The Board specifically found, at 1172, that the ALJ "erred" in failing to find that this rule unlawfully interfered with employees' statutory rights to bring their complaints to persons and entities other than the company, "including a union or the Board" even though the rule did not "on its face prohibit employees" from such actions. The Board further concluded, that the rule was unlawful because it "conflicts directly with the statutory policy of facilitating the ability of employees to organize and bargain collectively" and "tends to inhibit employees from banding together...." *Ibid.* [FN18]

Therefore, the employer also violated the Act by requiring employees to sign a copy of the rule, thus acknowledging their adherence to the rule. Id. at 1178.

The Employer also argues that the arbitration agreement merely requires an employee to use the Employer's arbitration procedure before filing charges and that it does not bar the employee from filing charges before the Board. Although the arbitration clause merely provided that employees must "first" seek redress of their claims through arbitration, theoretically permitting employees to exercise their statutory rights once the arbitration is concluded, such redress would be largely meaningless given the six-month statute of limitations in the NLRA and the time delays in getting cases decided by an arbitrator. Further, since the arbitration agreement specifically provides that employees must seek dismissal of any actions pending in other forums, the Employer has effectively thwarted any attempt to utilize a deferral or abeyance system in some other forum. Such language is a strong indication that the Employer's purpose in proposing this language was to preclude employees' access to alternative forums.

*6 Gilmer's reliance on the plaintiff's education and extensive business experience as evidence that he was not likely to be a victim of inequality of bargaining power between an individual and his employer is also inapposite in considering the merits of an unfair labor practice charge. Section 2(3) of the Act does not define protected employees in terms of education, experience or sophistication. Moreover, the Act specifically protects professional employees, including highly educated ones, as defined in Section 2(12). [FN19]

For all of the above reasons, we conclude that the Employer violated Section 8(a)(4) and (1) by insisting that, as a term and condition of employment, employees agree to waive their statutory rights to file charges with the Board. It follows that the Employer violated Section 8(a)(4) and (1) when it discharged Letwin because of his refusal to sign the agreement.

For all of the above reasons, a Section 8(a)(4) and (1) charge should issue, absent settlement. [FN22]

Barry J. Kearney

Acting Associate General Counsel

Division of Advice

FN1 Letwin has also filed a charge with the EEOC, alleging that his termination violated the Age Discrimination in Employment Act, 29 U.S.C. Sec. 621 et seq., and a civil suit under Florida law. These proceedings are pending.

FN2 The Section 8(a)(3) allegation should be dismissed, absent withdrawal. There is no evidence of any union activity on Letwin's part and any remedy which would be available under Section 8(a)(3) would also be available under Section 8(a)(1).

FN3 The House Conference Report No. 510 on H.R.3020 (the Taft-Hartley Act) reads:

The Senate amendment [to Section 10(a)], because of its provisions authorizing temporary injunctions enjoining alleged unfair labor practices and because of its provisions making unions usable, omitted the language giving the Board exclusive jurisdiction of unfair labor practices, but retained that which provides that the Board's power shall not be affected by any other means of adjustment or prevention. The conference agreement adopts the provisions of the Senate amendment. 1 Legislative History of the Labor Management Relations Act of 1947, p. 556.

FN4 309 U.S. 350 (1940).

FN5 Id. at 360. See also *J.I. Case v. NLRB*, 321 U.S. 332, 337 (1944), where the Supreme Court held that individual employment contracts were not a bar to the selection of a collective-bargaining representative, noting, "Wherever private contracts conflict with [the Act's] functions, they must obviously yield or the Act would be reduced to a futility."

FN6 See, e.g., *Kolman/Athey Division of Athey Products Corporation*, 303 NLRB 92 (1991); *Kinder-Care Learning Centers*, 299 NLRB 1171 (1990); *Great Lakes Chemical Corp.*, 298 NLRB 615, 622 (1990); *Retlaw Broadcasting Co.*, 310 NLRB 984 (1993).

FN7 *Construction and General Laborers, Local 304 (AGC of California)*, 265 NLRB 602 (1982).

FN8 299 NLRB at 1171.

FN9 Congress enacted Section 8(a)(4) to ensure that all persons would be "free from coercion against reporting [possible unfair labor practices] to the Board." *Nash v. Florida Industrial Commission*, 389 U.S. 235, 238 (1967).

FN10 Id. at 1651-52, fn. 2.

FN11 Ibid.

FN12 111 S.Ct. at 1655-56 (such claims will be resolved based on the facts of specific cases).

FN13 Id. at 1655.

FN14 Id. at 1656.

FN15 Id. at 1652, quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985).

FN16 See also *EEOC v. River Oaks Imaging and Diagnostic*, 67 FEP Cases 1243 (SD TX.1995), in which a federal court enjoined the employer from insisting that employees agree to an ADR (alternative dispute resolution) policy that would preclude or interfere with the employees' rights to file charges with the EEOC or file suits under Title VII, and would require employees to pay the costs of the ADR proceeding. The employer was also enjoined from retaliating against employees who filed complaints with the EEOC or opposed the employer's mandatory ADR policy. The EEOC and the employer subsequently agreed to a consent order consistent with the above injunction. The question of the lawfulness of the discharges of several employees was reserved for a trial de novo. See *Daily Labor Reporter*, July 3, 1995, at A-2. Neither the original injunction nor the consent order mention Gilmer.

The EEOC has since issued a policy statement stressing that any participation in ADR proceedings under the EEOC's auspices must be voluntary because "the unique importance of the laws against employment discrimination requires that a federal forum always be available to an aggrieved individual." "EEOC Policy Statement on Alternative Dispute Resolution," Number 915.002, *Daily Labor Reporter*, July 18, 1995, at E-13.

FN17 See, e.g., *A-1 King Size Sandwiches, Inc.*, 265 NLRB 850, 860 fn. 20 (1982), *enfd.* 732 F.2d 872 (11th Cir.1984), *cert. denied* 469 U.S. 1034, finding a grievance-arbitration provision "essentially illusory" because it did not apply to a sweeping list of management rights, including the right to discipline and discharge employees.

FN18 See also *Central Security Services*, 315 NLRB 239, 243, 253-54 (1994).

1995 WL 912536

(Cite as: 1995 WL 912536 (N.L.R.B.G.C.))

FN19 Compare OPEIU Local 2, 268 NLRB 1353, 1356 (1984), enf'd sub nom. Eichelberger v. NLRB, 765 F.2d 851 (9th Cir.1985), where, in find that a union did not breach its duty of fair representation in handling a grievance filed by an employee of the union, noted that the employee was thoroughly familiar with her contract rights, including the right to file a grievance without the union's participation, and had previously demonstrated an ability to exercise those rights.

Office of General Counsel

National Labor Relations Board (N.L.R.B.)

1995 WL 912536 (N.L.R.B.G.C.)

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**CLASS ACTIONS AND CLASS RELIEF:
THE BASICS & THE SPECIFICS
FOR EMPLOYMENT LAW**

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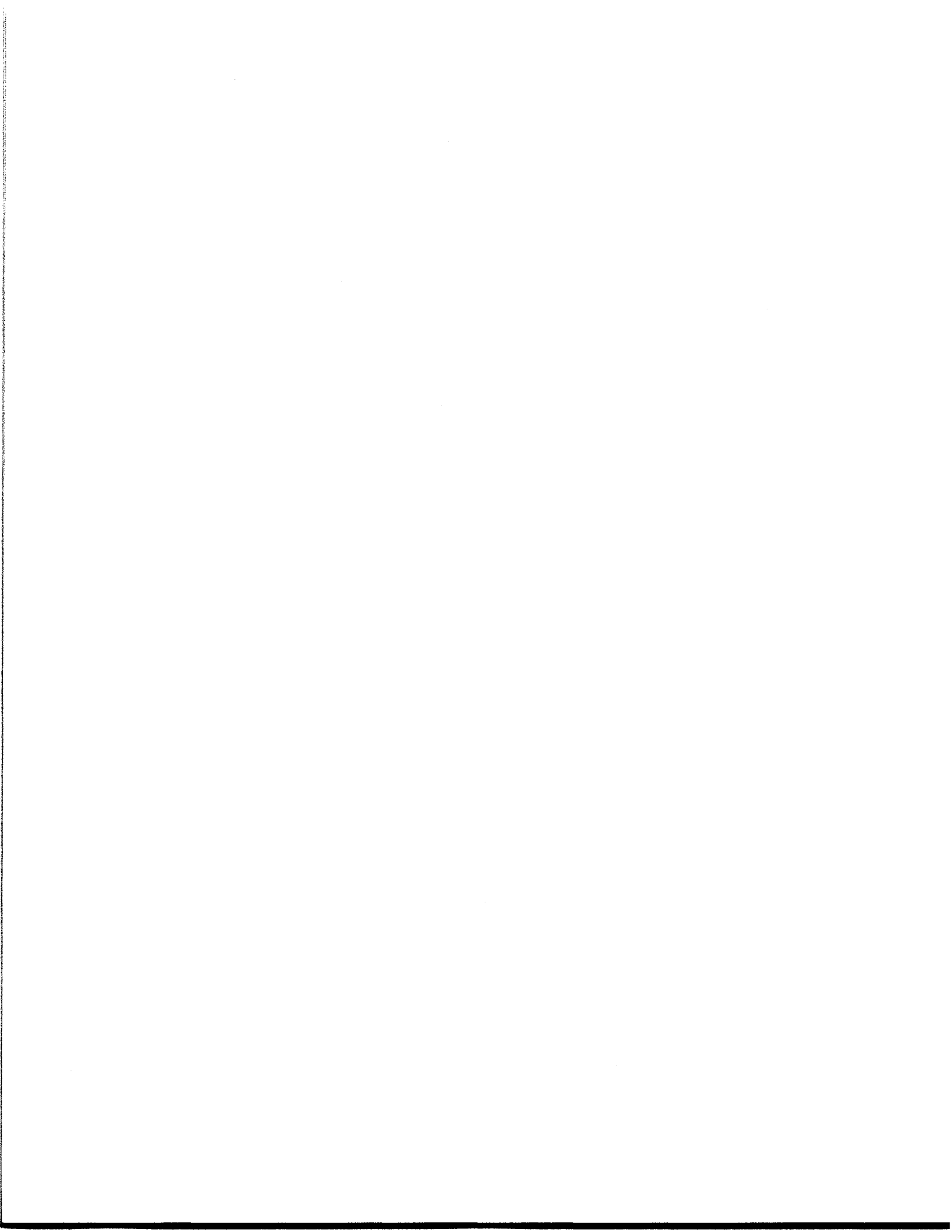
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SECTION J



**CLASS ACTIONS AND CLASS RELIEF:
THE BASICS AND THE SPECIFICS FOR EMPLOYMENT LAW**

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INTRODUCTION

It is not a news flash that employers today face an increasingly perilous landscape. In addition to the significant challenges that flow from a confusing economic picture, employers are faced with more frequent and dangerous claims by current and former employees. Among the claims that give rise to the biggest financial risk are those involving a request for class relief. For obvious reasons, employers want to do everything possible to avoid class exposure.

This outline will include a discussion of the fundamental requirements of a class action and the principal issues faced by parties when litigating employment law class actions. It will also include a brief discussion of emerging employment law issues in the class context.

BACKGROUND

A party may pursue a class action only if: (1) the class is so numerous that joinder of all members is impracticable (often abbreviated as “numerosity”); (2) there are questions of law or fact common to the class (often abbreviated as “commonality”); (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class (often abbreviated as “typicality”); and (4) the representative parties will fairly and adequately protect the interests of the class (often abbreviated as “fair and adequate representation”).¹ If all of these requirements are satisfied, the court may certify a class if, in addition, the class representatives meet any one of the following requirements:²

- (a) The prosecution of separate actions by or against individual members of the class would create a risk of:

¹ FRCP 23(a). Because a significant majority of class cases have been pursued in the federal courts, this outline focuses on class relief under federal law.

² These additional requirements are set forth in FRCP 23(b).

- (i) inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards of conduct for the party opposing the class; or
 - (ii) adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests; or
- (b) The party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole; or
- (c) The court finds³ that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy.⁴

The party seeking class certification bears the burden of proof⁵ and the class mechanism is not available merely because a lawyer designates a group of persons or entities as a “class” in the pleadings.⁶ Although a hearing prior to the class determination is not required in every instance, “it may be necessary for

³ The matters pertinent to these findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and (D) the difficulties likely to be encountered in the management of a class action. FRCP 23(b)(3).

⁴ The Supreme Court has held that district courts must conduct a “rigorous analysis” into whether the prerequisites of Rule 23 are met before certifying a class. General Tel. Co. v. Falcon, 457 U.S. 147, 161 (1982).

⁵ General Tel. Co. v. Falcon, 457 U.S. 147, 161 (1982).

⁶ Cash v. Swifton Land Corp., 434 F.2d 569, 571 (6th Cir. 1970).

the court to probe behind the pleadings before coming to rest on the certification question’ ”⁷ As the Sixth Circuit has noted:

Mere repetition of the language of Rule 23(a) is not sufficient. There must be an adequate statement of the basic facts to indicate that each requirement of the rule is fulfilled. Maintainability may be determined by the court on the basis of the pleadings, if sufficient facts are set forth, but ordinarily the determination should be predicated on more information than the pleadings will provideThe parties should be afforded an opportunity to present evidence on the maintainability of the class action.⁸

I. Rule 23 (a) requirements.

A. Numerosity.

As noted above, to satisfy FRCP 23(a), a party seeking class relief must demonstrate that the proposed class is so numerous that the joinder of all members is impracticable.⁹ The test for numerosity is not precise and involves an examination of the specific facts of each case.¹⁰ In determining whether joinder is impracticable, courts often will consider not only the size of the proposed class, but also “the class’s geographical dispersion, the ability of claimants to bring individual suits, and whether the members’ names are easily ascertainable.”¹¹ Even so, when the class size is extremely large, the impracticability requirement

⁷ In re American Medical Sys., 75 F.3d 1069, 1079 (6th Cir. 1996) (quoting General Tel. Co. v. Falcon, 457 U.S. at 160 (1982)).

⁸ Weathers v. Peters Realty Corp., 499 F.2d 1997, 1200 (6th Cir. 1974) (citation omitted).

⁹ FRCP 23(a)(1).

¹⁰ In re American Medical Sys., 75 F.3d 1069, 1079 (6th Cir. 1996).

¹¹ O’Neil v. Appeal, 165 F.R.D. 479, 489 (W.D. Mich. 1996).

is normally satisfied.¹² At least one court has concluded that fewer “than twenty-one [members] is inadequate, more than forty [is] adequate, with numbers between varying according to other factors.”¹³

It is important to note that mere conclusory allegations that joinder is impracticable are not sufficient to satisfy the numerosity requirement.¹⁴ Indeed, it is proper for a court to rule against class certification when the contentions concerning the size of the class are purely speculative.¹⁵

As with all of the requirements of class status, a claimant typically must establish the numerosity requirement by a preponderance of the evidence.¹⁶

B. Commonality.

A party seeking class status must prove that there are questions of law or fact common to the class.¹⁷ Although a claimant can satisfy this requirement even if the claims are not identical, when the resolution of a common legal issue is dependent upon factual determinations that will be different for each purported class member, the courts have consistently refused to find that the commonality

¹² In re American Medical Sys., 75 F.3d 1069, 1079 (6th Cir. 1996). See also Ilhardt v. A.O. Smith Corp., 168 F.R.D. 613, 617 (S.D. Ohio 1996) (“Numerosity may be satisfied by numbers alone”).

¹³ N.A.A.C.P. v. City of Thomasville School Dist., 187 F.R.D. 690, 696 (M.D. Ga. 1999) (quoting Cox v. American Cast Iron Pipe Co., 784 F.2d 1546, 1553 (11th Cir. 1986)).

¹⁴ See Liberty Lincoln Mercury, Inc. v. Ford Marketing Corp., 149 F.R.D. 65, 74 (D. N.J. 1993).

¹⁵ Vigue v. Ives, 138 F.R.D. 6, 8, (D. Maine 1991).

¹⁶ Ilhardt v. A.O. Smith Corp., 168 F.R.D. 613, 618 (S.D. Ohio 1996).

¹⁷ FRCP 23(a)(2).

requirement was satisfied.¹⁸ Thus, where there is a finding that common issues do not predominate, certification is improper.¹⁹

The Sixth Circuit has noted that the “commonality requirement is interdependent with the impracticability of joinder requirement, and the ‘tests together form the underlying conceptual basis supporting class actions’ ”.²⁰

C. Typicality.

To meet the typicality requirement, the party seeking class status must establish that the claims or defenses of the representative party are typical of the claims or defenses of the class.²¹ Stated otherwise, the class representative’s interests must be aligned with those of the represented group so that “in pursuing his own claims, the named plaintiff will be advancing the interests of the class members.”²² This test is normally met as long as there is “a nexus between the class representatives’ claims” and the common questions of fact or law concerning the class.²³ If there is a defense that is peculiar to the named plaintiff, class certification may be denied.²⁴

¹⁸ See, e.g., Liberty Lincoln Mercury, Inc. v. Ford Marketing Corp., 149 F.R.D. 65, 76 (D.N.J. 1993). See also McCauley v. International Business Machines, 165 F.3d 1038, 1046-47 (6th Cir. 1999) (holding that to meet the commonality requirement, the allegations of misrepresentations upon which the class claims are based must “be uniform among class members”)

¹⁹ In re American Medical Sys., 75 F.3d 1069, 1085 (6th Cir. 1996) (“[T]he products are different, each plaintiff has a unique complaint, and each received different information and assurances from his treating physician”).

²⁰ In re American Medical Sys., 75 F.3d 1069, 1080 (6th Cir. 1996) (quoting 1 Newberg on Class Action, § 3.10, at 3-47).

²¹ FRCP 23(a)(3).

²² In re American Medical Sys., 75 F.3d 1069, 1082 (6th Cir. 1996).

²³ Cook v. Rockwell International Corp., 151 F.R.D. 378, 385 (D. Colo. 1993).

²⁴ Ballan v. Upjohn Co., 473 F.R.D. 473, 480 (W.D. Mich. 1994).

D. Adequacy of Representation.

Whether representation is adequate is generally considered a question of fact based upon the circumstances of each case.²⁵ For a representative to meet the test: (a) he or she must have common interests with the unnamed members of a class; and (b) it must appear that the representative will vigorously prosecute the interests of a class through qualified counsel.²⁶ Applying these factors, courts will review whether there is any antagonism between the interests of the named plaintiff and the other members of the class and also review the experience and the ability of the attorneys for the class.²⁷ In addition, the class representative must “ ‘posses the same interest and suffer the same injury’ as the class members.”²⁸ With respect to that point, a person will not be deemed an adequate class representative if he or she fails to establish the existence of a case or controversy.²⁹ Moreover, standing must exist both at the time the complaint is filed and at the time the class is certified.³⁰

On a similar point, special mootness rules exist for class actions. Once a class is certified, “the mooting of the named plaintiff’s claim does not moot the action” and “the court continues to have jurisdiction to hear the merits of the

²⁵ Id. at 482.

²⁶ In re American Medical Sys., 75 F.3d 1069, 1083 (6th Cir 1996).

²⁷ Ballan v. Upjohn Co., 159 F.R.D. 473, 482 (W.D. Mich. 1994).

²⁸ General Tel. Co. v. Falcon, 457 U.S. 147, 156 (1982); James v. Jones, 148 F.R.D. 196, 201 (W.D. Ky. 1993).

²⁹ Coleman v. Cannon Oil Co., 141 F.R.D. 516, 523 (M.D. Ala. 1992).

³⁰ Brunet v. City of Columbus, 1 F.3d 390, 399 (6th Cir. 1993).

action if a controversy between any class member and the defendant exists.”³¹ On the other hand, where the named plaintiff’s claim becomes moot before certification, dismissal of the action is required.³²

II. Rule 23(b) Requirements.

As discussed above, a party seeking class relief may pursue a class action if he or she meets the Rule 23(a) “prerequisites” and, in addition, demonstrates the applicability of one of the three subparts of Rule 23(b).

A. Risks From Prosecution of Separate Actions.

Rule 23(b)(1) recognizes the propriety of a class action if the Rule 23(a) prerequisites are met and the prosecution of separation action by or against individual members of the class would create a risk of: (a) inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards for the party opposing the class; or (b) adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests. A judgment in a Rule 23(b)(1) case “shall” include and describe those whom the court finds to be members of the class.³³

B. Conduct Giving Rise to Injunctive or Declaratory Relief.

Under Rule 23(b)(2), class relief will be deemed proper if the Rule 23(a) prerequisites are satisfied and the party opposing the class has acted or refused to

³¹ Brunet v. City of Columbus, 1 F.3d 390, 399 (6th Cir. 1993).

³² Id.

³³ FRCP 23(c)(3). This same requirement applies to a judgment entered in a Rule 23(b)(2) class action.

act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole.

C. Predominance of Common Questions.

Class relief is appropriate under the last subpart of Rule 23(b) if the Rule 23(a) prerequisites are satisfied and the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy.³⁴ The Rule specifically identifies the following list of factors that are “pertinent to the findings”: (a) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (b) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (c) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and (d) the difficulties likely to be encountered in the management of a class action.³⁵

With respect to a FRCP 23(b)(3) class action, the court is required to direct to the members of the class the “best notice practicable under the circumstances”, including individual notice to all members who can be identified through reasonable effort.³⁶ Such notice “shall” advise each member that: (a) the court will exclude the member from the class if the member so requests by a

³⁴ FRCP 23(b)(3).

³⁵ Id.

³⁶ FRCP 23(c)(2).

specified date; (b) the judgment, whether favorable or not, will include all members who do not request exclusion; and (c) any member who does not request exclusion may, if the member desires, enter an appearance through counsel.³⁷ Due process concerns mandate the opt-out mechanism.³⁸

A judgment entered in a Rule 23(b)(3) case “shall” include and specify or describe those to whom the notice provided in the preceding paragraph was directed, and who have not requested exclusion, and whom the court finds to be members of the class.³⁹

Issues of damages in a Rule 23(b)(3) action may, where appropriate, be reserved for individual treatment, with the question of liability tried as a class action.⁴⁰ In complex cases where no single set of operative facts establishes liability, where no single proximate cause applies to each potential class members and to each defendant, and where individual issues outnumber common issues, however, the district court should question the appropriateness of a class action for resolving the controversy.⁴¹

III. Other Procedures.

A. Class Certification.

Rule 23 specifically provides that “[a]s soon as practicable after the commencement of an action brought as a class action, the court shall determine by

³⁷ Id.

³⁸ Becherer v. Merrill Lynch, Pierce, Fenner and Smith, Inc., 193 F.3d 415, 425 (6th Cir. 1999).

³⁹ FRCP 23(c)(3).

⁴⁰ Ilhardt v. A.O. Smith Corp., 168 F.R.D. 613, 619 (S.D. Ohio 1996).

⁴¹ Id.

order whether it is to be so maintained.”⁴² Providing the court a measure of flexibility, the Rule also provides that “[a]n order under this subdivision may be conditional, and may be altered or amended before the decision on the merits.”⁴³ In the Sixth Circuit, there is an abuse of discretion standard for the review of a trial court’s class action certification.⁴⁴ In addition, if the parties agree to class certification or if the opposing party does not contest the assertions of the party seeking class certification as to the existence of a prerequisite, the district court may conclude that certification is proper or that the prerequisites are properly established without making a specific finding.⁴⁵

B. Discrete Issues and Subclasses.

Rule 23 explicitly recognizes that an action may be brought or maintained as a class action with respect to particular issues.⁴⁶ Similarly, a class may be divided into subclasses and each subclass treated as a class.⁴⁷

C. Orders in Conduct of Actions.

Rule 23 provides that a court in a class action may make appropriate orders: (1) determining the course of proceedings or prescribing measures to prevent undue repetition or complication in the presentation of evidence or argument; (2) requiring, for the protection of the members of the class or

⁴² FRCP 23(c)(1).

⁴³ Id.

⁴⁴ McCauley v. International Business Machines Corp., 165 F.3d 1038, 1046 (6th Cir. 1999).

⁴⁵ In re American Medical Sys., 75 F.3d 1069, 1079-80 (6th Cir. 1996).

⁴⁶ FRCP 23(c)(4).

⁴⁷ Id.

otherwise for the fair conduct of the action, that notice be given in such manner as the court may direct to some or all of the members of any step in the action, or of the proposed extent of the judgment, or of the opportunity of the members to signify whether they consider the representation fair and adequate, to intervene and present claims or defenses, or otherwise to come into the action; (3) imposing conditions on the representative parties or on intervenors; (4) requiring that the pleadings be amended to eliminate therefrom allegations as to representation of absent persons, and that the action proceed accordingly; (5) dealing with similar procedural matters.⁴⁸

D. Dismissal or Compromise.

A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs.⁴⁹

E. Appeals.

A court of appeals may in its discretion permit an appeal from an order of a district court granting or denying class action certification under the Rule if application is made to it within ten days after entry of the order.⁵⁰ An appeal does not stay proceedings in the district court unless the district judge or the court of appeals so orders.⁵¹

⁴⁸ FRCP 23(d).

⁴⁹ FRCP 23(e).

⁵⁰ FRCP 23(f). It is noteworthy that there is no corresponding provision under Rule 23 of the Kentucky Rules of Civil Procedure.

⁵¹ Id.

IV. Emerging Class Issues in Employment Law.

A. Claims Regarding Employee Benefits.

Among the most prevalent class action claims in the employment law area are those regarding employee benefits.⁵² Such claims typically are pursued under the Federal Employee Retirement Income Security Act (“ERISA”).⁵³ Class claims under ERISA may involve such issues as “nondisclosure, breach of duty, or nonforfeiture provisions.”⁵⁴

B. Discrimination Claims.

Employers today face an increasing risk of defending discrimination claims by groups of former, or even current, employees. In earlier cases under Title VII of the Civil Rights Act of 1964, many courts tended to be more lenient in finding compliance with Rule 23 than in other types of cases.⁵⁵ That tendency ended after the United States Supreme Court emphasized that a Title VII class plaintiff must satisfy all of the requirements of Rule 23,⁵⁶ noting:

We are not unaware that suits alleging racial or ethnic discrimination are often by their very nature class suits, involving classwide wrongs. Common questions of law or facts are typically present. But careful attention to the requirements of Fed. Rule Civ. Proc. 23 remains nonetheless indispensable. The mere fact that a complaint alleges racial or ethnic discrimination does not in itself ensure that the party who has brought the lawsuit will be an adequate representative

⁵² This topic has been addressed extensively by other speakers.

⁵³ 29 U.S.C. § 1001, et. seq.

⁵⁴ 5 James Wm. Moore, et al. Moore’s Federal Practice § 23.23 [5][i] (3d ed. 2000).

⁵⁵ Lindemann & Grossman, Employment Discrimination Law, Vol. II at 1582 (3d ed. 1996).

⁵⁶ East Texas Motor Freight System, Inc. v. Rodrigues, 431 U.S. 395 (1977).

of those who may have been the real victims of that discrimination.⁵⁷

As a general proposition, disparate treatment discrimination claims are often not appropriate for class treatment because allegations of intentional discrimination often raise individual issues.⁵⁸ Stated another way, “[i]t is more difficult to find commonality and typicality in disparate treatment claims as opposed to disparate impact claims.”⁵⁹ Among the problems with the pursuit of disparate treatment class claims is that the recovery of compensatory and punitive damages in Title VII cases “requires individualized and independent proof of injury to, and the means by which discrimination was inflicted upon, each class member.”⁶⁰ As the United States Court of Appeals for the Fifth Circuit has noted:

The plaintiffs’ claims for compensatory and punitive damages must therefore focus almost entirely on facts and issues specific to individuals rather than the class as a whole: what kind of discrimination was each plaintiff subjected to; how did it affect each plaintiff emotionally and physically, at work and at home; what medical treatment did each plaintiff receive and at what expense; and so on and so on. Under such circumstances, an action conducted nominally as a class action would ‘degenerate in practice into multiple lawsuits separately tried.’⁶¹

A Title VII plaintiff bringing a disparate impact claim must identify a specific practice or specific practices as the cause of the alleged impact, unless the

⁵⁷ Id. at 405-06.

⁵⁸ Lindemann & Grossman, n. 55, supra, at 1593.

⁵⁹ Carter v. West Publishing Co., 79 FEP 1494, 1498 (D. Fla. 1999). See also Zachery v. Texaco Exploration & Prod., Inc., 185 F.R.D. 230, 239 (W.D. Tex. 1999) (“Because disparate treatment claims are by their nature individual, the class treatment of these claims requires close scrutiny of the proposed class and claims.”).

⁶⁰ Allison v. Citgo Petroleum Corp., 151 F.3d 402, 419 (5th Cir. 1998).

⁶¹ Id.

elements of the decision making process are not capable of separation for analysis.⁶² Courts generally find the Rule 23(a) requirements met in disparate impact cases when the plaintiffs identify a particular test or other objective selection devise that created the disparate impact.⁶³

C. Harassment Claims.

Although harassment claims more often than not involve allegations of individual harassment, there is precedent for class actions that arise from an alleged pervasive course of harassing conduct affecting a large number of persons.⁶⁴

D. Wage and Hour Claims.

Wage and hour claims, like those asserted under ERISA, can give rise to significant exposure for relatively minor missteps. Under Federal Law,⁶⁵ there are special rules concerning collective claims that, in contrast to those in Rule 23, require claimants to opt in to a potential class.⁶⁶ Oddly, the Kentucky Wage and Hour chapter, though based in significant part on the Fair Labor Standards Act, does not explicitly contain a similar “opt in” provision.⁶⁷

⁶² Lindemann & Grossman, n. 55, supra, at 1591.

⁶³ Id., 2000 cum. supp. at 881.

⁶⁴ See, e.g., Donnelly v. Glickman, 159 F.3d 405 (9th Cir. 1998).

⁶⁵ The Fair Labor Standards Act, 29 U.S.C. section 201, et seq. requires payment of minimum wages and overtime to employees covered by the Act.

⁶⁶ 29 U.S.C. § 216 (“No employee shall be a party plaintiff to any such action unless he gives his consent in writing to become such a party and such consent is filed in the court in which such action is brought.”).

⁶⁷ See KRS 337.385 (“Such action may be maintained in any court of competent jurisdiction by any one (1) or more employees for and in behalf of themselves.”).

THE EMPLOYEE AT-WILL DOCTRINE IN KENTUCKY

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SECTION K

THE EMPLOYEE AT-WILL DOCTRINE IN KENTUCKY©

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THE EMPLOYEE AT-WILL DOCTRINE IN KENTUCKY

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Although many employees in Kentucky still find it surprising, under the doctrine of employment at-will, a person's employment generally may be terminated at any time, with or without notice, for any reason or no reason at all. Of course, employees also have the right to end their employment at any time and for any reason or no reason at all. This doctrine is simple in appearance, but not in application due to ever increasing exceptions to it. This paper explores the current state of the employment at-will doctrine in Kentucky and comments on its future.

HISTORY

The doctrine of employment at-will can be traced to the Middle Ages. In 1349, King Edward III of England promulgated the Statute of Labourers to alleviate labor shortages caused by the Black Death, a bubonic plague that killed nearly half of the population of Great Britain. The Statute compelled workers to accept employment at wages as they existed prior to the Black Death. It also prohibited workers from quitting before the end of the agreed-upon employment term. Workers who departed before the agreed-upon time of service were imprisoned.¹

The Statute of Labourers controlled until 1562, when Queen Elizabeth I promulgated the Statute of Artificers. Like the Statute of Labourers, the impetus for the Statute of Artificers was a plague, this one reducing England's population by five percent. The law was designed to prevent employers from hiring laborers only during harvesting season, and then dismissing them during winter months. It was also designed to prevent laborers from leaving their employment just before the most difficult time of the year. To that end, employment for industrial and agricultural workers was mandated to be for at least one year. The statute provided a loophole, however, for leaving employment in the case of "some reasonable and sufficient cause or matter to be allowed before two justices of the peace, or one at the least, within the said county...."²

¹ William, Schwab, and Burton, Employment Law, (2d ed. 1998), pp. 49-50.

² *Id.* at 50-51.

The Statute of Artificers remained in force until it was formally repealed in 1875. During this time, William Blackstone authored his now-famous rule on employment that was for no specified period of time. In his *Commentaries* (1765), Blackstone stated: “If the hiring be general without any particular time limited, the law construes it to be a hiring for a year; upon a principle of natural equity that the servant shall serve, and the master maintain him, throughout all the revolutions of the respective seasons, as well when there is work to be done, as when there is not: but the contract may be made for any longer or smaller term.” Again, the rule was designed to prevent employers from dismissing laborers during the off-season, and to prevent laborers from leaving their work before the hardest part of the year.

As England and the United States moved away from an agrarian economy, and toward an industrial economy, the one-year employment rule began to make less sense. Accordingly, courts began to develop the at-will employment doctrine. The earliest mention in Kentucky of something similar to this rule appeared at the end of the 19th century in *Louisville & Nashville Railroad Company v. Harvey*, 34 S.W. 1069 (Ky. 1896), which noted the general rule in Kentucky that an employment contract, in the absence of a specific agreement concerning duration, is terminable at-will. This rule solidified as Kentucky dealt with the Great Depression. See *Clay v. Louisville & Nashville Railroad Company*, 71 S.W.2d 617 (Ky. 1934); *Western Union Telegraph Company v. Ramsey*, 88 S.W.2d 675 (Ky. 1935).

THE DOCTRINE

The most popular current statement of the employment at-will doctrine in Kentucky comes from *Firestone Textile Company Division, Firestone Tire & Rubber Company v. Meadows*, 666 S.W.2d 730, 731 (Ky. 1983), where the Court stated: “ordinarily an employer

may discharge his at-will employee for good cause, for no cause, or for a cause that some might view as morally indefensible.”

One should always acknowledge that **every** employment relationship is contractual, even if that contract is terminable at-will. See, Richard A. Bales and Joseph S. Burns, *A Survey of Kentucky Employment Law*, 28 Northern Kentucky Law Review 219, 220 (2001). This point is often lost on employers, employees and scholars.

The doctrine of employment at-will is really no different from the ordinary contract law rule that a contract which does not specify its duration is terminable at the will of either party. See KRS § 355.2-309(2) (Article 2, Part 3 of the Uniform Commercial Code, governing “general obligation and construction of contract”); *Kirby v. Scroggins*, 246 S.W.2d 453 (Ky. 1952). It simply would be too much work for courts to guess at what the parties intended the duration of every indefinite contract to be. Thus, to preserve judicial resources, courts allow contracts of indefinite duration to be cancelled by either party at any time.

The at-will employment doctrine applies this principle to contracts for employment. (Remember, all employment relationships are contractual). Thus, when an employer and employee enter into an employment relationship for an indefinite duration, both parties have the privilege of ending the relationship at any time and for any reason, subject to many exceptions.

Employees are often surprised to learn they can be terminated without a good reason. Courts sometimes attempt to mollify angry plaintiffs by explaining the benefits of the rule. See *MacKenzie v. Miller Brewing Company*, 2001 WL 273843 (Wis. 2001). Commentators have similarly tried to justify the rule:

The employment at-will doctrine derives its vitality from the fact that the future is unknowable. Although the employee may tell his or her employer that he/she will be available for a certain period of

time, subsequent events may cause the employee to leave, either to pursue an opportunity elsewhere or for some personal reason.

Similarly, an employer may be unable to project what will happen in the future.

The future is not clearly known. More important, employees, like employers, know what they do not know. They are not faced with a bolt from the blue, with an “unknown unknown.” Rather they face a known unknown for which they can plan. The at-will contract is an essential part of that planning because it allows both sides to take a wait-and-see attitude to that relationship so that new and more accurate choices can be made on the strength of improved information.

Richard A. Epstein, *In Defense of the Contract At-Will*, 51 University of Chicago Law Review 947, 969 (1984).

EXCEPTIONS TO THE AT-WILL DOCTRINE

It is dangerous for an employer to believe it always has the right to terminate an at-will employee for “no cause,” or for a “morally indefensible” cause. Several exceptions to the at-will doctrine have been created by the Kentucky General Assembly. The broadest of these exceptions is found in the Kentucky Civil Rights Act, KRS Chapter 344, which makes it unlawful for an employer “To fail or refuse to hire, or to discharge any individual, or otherwise to discriminate against an individual with respect to compensation, terms, conditions, or privileges of employment, because of the individual’s race, color, religion, national origin, sex, age forty (40) and over, because the person is a qualified individual with a disability, or because the individual is a smoker or nonsmoker, as long as the person complies with any workplace policy concerning smoking....” KRS § 344.040. This statute prohibits essentially the same discriminatory termination as its federal equivalent, Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e, *et seq.* See also 42 U.S.C. § 621 *et seq.* (Age Discrimination in Employment Act) and 42 U.S.C. § 12101 *et seq.* (Americans with Disabilities Act).

The Kentucky Civil Rights Act and the Federal Civil Rights Act, by their express language, limit the circumstances under which an employer can discharge an employee. These limitations become very apparent when one considers the burden of proof under these statutes. Under the well known case of *McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973), a plaintiff establishes a *prima facie* case of discrimination by demonstrating that (1) s/he belongs to a protected category, (2) s/he was qualified for the job that he or she sought or held, (3) s/he suffered an adverse employment action, and (4) the position remained open and the employer continued to seek applicants. Obviously, this burden of proof is minimal.

Most employees who fall into one of the protected categories listed in Title VII or KRS Chapter 344 will be able to meet the burden. Once the *prima facie* case has been established, the burden then shifts to the employer to articulate a legitimate, non-discriminatory reason for the adverse employment action. In other words, if an employee falls into one of the protected categories of the civil rights acts, and the employee is discharged (or suffers some other adverse employment action), an employer must generally have a legitimate, non-discriminatory reason for the discharge if the employer wishes to avoid liability. *McDonnell Douglas*, 411 U.S. at 802-3. This requirement – that the employer have a legitimate, non-discriminatory reason for discharging employees in protected groups – undercuts the employment at-will doctrine.

Other statutes have further eroded the employment at-will rule. KRS § 342.197 prohibits an employer from retaliating against an employee who pursues a worker's compensation claim. A plaintiff relying on this statute for a cause of action must show that (1) s/he engaged in statutorily protected activity, (2) s/he was discharged, and (3) there is a causal connection between the protected activity and the discharge. A causal connection can be established by demonstrating a retaliatory reason for the discharge "was a substantial and motivating factor" in

the decision to terminate the employee: *First Property Management Corp. v. Zarebidaki*, 867 S.W.2d 185, 188 (Ky. 1993). An employer may not evade liability by showing that the discharge would have occurred even absent the retaliatory motive. *Id.* However, if the employer can demonstrate that the employee was discharged as a result of – for example – a neutral attendance policy, the plaintiff will not succeed in demonstrating the requisite causal connection. *Daniels v. R. E. Michel Company, Inc.*, 941 F.Supp. 629 (E.D. Ky. 1996).

Kentucky has also passed a statute protecting public employees against discharge in retaliation for disclosures of violations of the law. The so-called “whistleblower” statute, KRS § 61.101 *et seq.*, prohibits discharge or other retaliation against a public employee who, in good faith, reports an actual or suspected violation of any law, statute, executive order, administrative regulation, or rule of the federal or state government. KRS § 61.102. Employees are also covered if they make disclosure on behalf of another employee. KRS § 61.103. The statute specifically allows employees to bring a civil action for appropriate injunctive relief or punitive damages, or both. KRS § 61.103(2). Employees need only show that their disclosure was a contributing factor to their discharge in order to succeed. The burden then shifts to the employer to show by “clear and convincing” evidence that the disclosure was not a material factor in the discharge. KRS § 61.103(3).

Kentucky courts have also created exceptions to the at-will doctrine. The most common exception created by the courts provides an employee with a cause of action for “wrongful discharge.” This cause of action is a favorite with employees because it supports the general misconception that employees have the right to keep their job so long as they are doing a “good” job.

The tort of wrongful discharge first appeared in Kentucky in *Firestone Textile Company Division, Firestone Tire & Rubber Company v. Meadows*, 666 S.W.2d 730, 732 (Ky. 1983), where the court held an employee has a cause of action for wrongful termination where his or her discharge is contrary to a “public policy [which] must be evidenced by a constitutional or statutory provision.” *Firestone*, 666 S.W.2d at 731 (emphasis added). The court recognized that KRS Chapter 342, the Kentucky Worker’s Compensation Statute, contains just such a policy. (*Firestone* predated the enactment of KRS 342.197). An employee must “be free to assert a lawful claim for benefits without suffering retaliatory discharge.” *Id.* at 731. According to the court, “the only effective way to prevent an employer from interfering with his employees’ rights to seek compensation is to recognize that the latter has a cause of action for retaliatory discharge when the discharge is motivated by the desire to punish the employee for seeking the benefits to which he is entitled by law.” *Id.* at 734. Justice Stephenson dissented, believing the *Firestone* decision would begin the abandonment of the employment at-will doctrine because a good lawyer could “always find a right implicit in the statute....” *Id.* at 734.

Two years later, however, the court clearly delineated and limited the *Firestone* public policy exception to the employment at-will doctrine:

1. The discharge must be contrary to a fundamental and well-defined public policy as evidenced by existing law.
2. That policy must be evidenced by a constitutional or statutory provision.
3. The decision of whether the public policy asserted meets these criteria is a question of law for the court to decide, not a question of facts.

Grzyb v. Evans, 700 S.W.2d 399, 401 (Ky. 1985). In *Grzyb*, the plaintiff had alleged wrongful discharge, and had alleged a public policy against sex discrimination³ to form the basis of her

³ The Plaintiff’s complaint in *Grzyb* did not explicitly reference KRS Chapter 344; it merely alleged that the plaintiff was fired for fraternizing with a female employee. The Court assumed, for the purposes of argument, that

argument. Importantly, the court held this was impermissible. KRS Chapter 344 not only created the public policy upon which the plaintiff relied, but it also pre-empted the field of its application. According to the court, “where the statute both declares the unlawful act and specifies the civil remedy available to the aggrieved party, the aggrieved party is limited to the remedy provided by the statute.” *Grzyb*, 700 S.W.2d at 401. Thus, in Kentucky, an employee cannot base a wrongful discharge claim on a public policy set forth in a statute that also specifies a civil remedy.

Less than a decade later, the Kentucky Supreme Court again whittled away at the *Firestone* decision. In *Boykins v. Housing Authority of Louisville*, 842 S.W.2d 527 (Ky. 1992), the court limited the type of statutory or constitutional policy that can form the basis of a wrongful discharge claim. The plaintiff, Karen Boykins, was employed as an executive secretary by the Housing Authority of Louisville. Her infant son was allegedly injured in an apartment owned, operated, and managed by the Housing Authority. Boykins filed a negligence suit on behalf of her son, and was subsequently fired by the Housing Authority. She then brought a second suit, this time in her own name, alleging retaliatory discharge for having brought the first lawsuit. She based her claim for wrongful discharge on the “open courts” provision of the Kentucky Constitution. Kentucky Constitution, Section 14. The court rejected this claim. Reasoning that the “open court” provision has nothing to do with employment rights, the court denied Boykins’ claim because there is no “employment-related nexus between the constitutional policy stated in Section 14 and Boykin’s discharge.” *Boykins*, 842 S.W.2d at 530. Thus, in Kentucky, for a wrongful discharge claim to succeed, the constitutional or statutory provision upon which the plaintiff relies must have an “employment-related nexus” to the employee’s discharge.

the complaint sufficiently alleged sex discrimination.

Despite the existence of a cause of action for wrongful discharge, the law imposes no obligation on employers to treat employees with "good faith." Nearly every other contractual relationship has an implied duty of good faith and fair dealing on the part of all parties to the contract. However, this is not the case with the employment contract. In *Wyant v. SCM Corporation*, 692 S.W.2d 814 (Ky.App. 1985), an employee sought to recover against his former employer for wrongful discharge, as well as bad faith and defamation. The court dismissed the employee's wrongful discharge and defamation claims with little discussion. On the claim of bad faith, the court dealt with the employee's argument that his 17-year tenure with the company imposed an implied duty of good faith and fair dealing upon his employer. The court rejected this argument as being inconsistent with the doctrine of employment at-will. After all, if an employer can end an employee's employment at any time, and for any reason, an implied duty of good faith in an employment contract would render the at-will doctrine meaningless. Thus, in Kentucky, there is no cause of action for breach of the duty of good faith and fair dealing in an employment contract.

FURTHER MODIFICATION

Aside from the rather narrow exception to the employment at-will doctrine provided by the tort of wrongful discharge, there exist several other ways in which the parties may modify their at-will relationship. The most obvious way is through contract. Since even an at-will employment relationship is a contractual one, both parties may agree that the rule of at-will employment will not apply. Modification of the employment at-will relationship may be either oral or written. Also, even if the parties do not agree on a specified duration for the employment relationship, the parties may still agree that the relationship is terminable only for cause.

The seminal case in Kentucky on contractual modification of the employment at-will doctrine is *Shah v. American Synthetic Rubber Corporation*, 655 S.W.2d 489 (Ky. 1983). American Synthetic recruited Shah from a job in St. Louis, Missouri. According to Shah, he relied on various sales pitches from American Synthetic designed to induce him to relocate to Kentucky. As part of these sales pitches, Shah alleged that he and American Synthetic agreed, among other things, to an employment contract under which Shah would serve a 90-day probationary period. During the probationary period, American Synthetic could discharge him for any cause whatsoever. After the 90 days had elapsed, Shah alleged that he became a permanent employee dischargeable only for cause in accordance with the personnel policies and procedures established by American Synthetic. "For cause" was defined by one of American Synthetic's personnel managers as "something like work connected performance, insubordination, violation of policy or rules, or lack of work." *Shah*, 655 S.W.2d at 491.

Shah was fired after the 90-day probationary period, and he brought suit against American Synthetic. The trial court held that Shah's employment was for an indefinite period of time and, therefore, was terminable at-will. The court granted summary judgment for American Synthetic, but the Kentucky Supreme Court reversed. According to the Supreme Court, parties may enter into a contract of employment terminable only pursuant to its express terms. So long as parties clearly state their intention to enter into such a contract, it is valid "even though no other consideration than services to be performed are promised, is expected by the employer, or performed or promised by the employee." *Shah*, 655 S.W.2d at 492. The court remanded for a determination of whether Shah's employment contract contained a clause permitting his termination only for cause, or whether he was fired in accordance with company policies and procedures.

An employee faced a similar situation in *Hammond v. Heritage Communications, Inc.*, 756 S.W.2d 152 (Ky.App. 1988). The plaintiff was an employee of two radio stations in Barren County, Kentucky. Both stations were owned by the defendant. Plaintiff specifically alleged that she was encouraged by her employer to appear in *Playboy* magazine. At the very least, her supervisor told her that she would not lose her job if her photograph were to appear in the magazine. After her photograph was published, she was terminated. She brought suit, alleging wrongful discharge and breach of an oral contract. On appeal, the court focused on the plaintiff's argument that an oral contract had been created. The record was undisputed that the plaintiff's supervisor told her that she would not lose her job if her photograph appeared in *Playboy*. The Court of Appeals held that this fact made summary judgment inappropriate. Plaintiff was entitled to establish that her at-will status was altered by the oral assurances she received from her supervisor. A reasonable jury could find that an oral contract existed, which the company breached by terminating the plaintiff.

The at-will employment relationship may also be modified by employee handbooks and policies. In *Nork v. Fetter Printing Company*, 738 S.W.2d 824 (Ky.App. 1987), several cases⁴ were appealed simultaneously which presented common material facts and issues relating to wrongful discharge claims. In each case, the employee and the employer operated under an employee manual or handbook which set forth personnel policies. Each plaintiff argued that these handbooks altered the at-will employment relationship by manifesting an expression of contractual agreement. However, in each case, the employee handbook contained a clear disclaimer stating that it was not intended to be a contract. Each handbook contained a statement that the parties' relationship was intended to be "at-will." The court relied heavily upon these

⁴ *Nork, Scheurich v. Cross Motors Corp.* and *Baker v. Slack* were consolidated.

statements. Since the parties did not mutually intend to modify the at-will relationship, the court entered summary judgment for each employer.

The Kentucky Court of Appeals reached a similar decision in *Noel v. Elk Brand Manufacturing Company*, 53 S.W.3d 95 (Ky.App. 2000). The parties in *Noel* operated under an employee handbook that did not expressly provide that the employees were at-will employees. The handbook did specifically state that employees could rely on the company for wages, benefits, holidays, and seniority. The plaintiff argued that this handbook abrogated the default rule of at-will employment. However, the court rejected the plaintiff's arguments because the employee handbook specifically provided that it was "not a contract." *Noel*, 53 S.W.3d at 99. Thus, while the disclaimer in the Elk Brand handbook was different from the one in the *Nork* case, the court still held that the disclaimer was effective to prevent the handbook from modifying the at-will employment relationship. Caveat: Employers are advised to include the full "at-will" disclaimer in all applications and handbooks.

In addition to their reliance on employee handbooks, employees sometimes argue that the at-will employment relationship has been modified by looking to written or oral offers of employment, and to statements of an employee's compensation. For example, an offer letter that indicates an employee will be employed at a wage rate of "\$40,000.00 per year" can be construed as an offer of one year employment. Similarly, an offer to employ someone for a 90-day probationary period could also be construed as an offer to provide employment for a minimum of 90 days, or to provide permanent employment after the expiration of the 90 days. Statements like these can unintentionally create contracts for a specific duration. See *Putnam v. Producer's Livestock Marketing Ass'n.*, 75 S.W.2d 1075 (Ky. 1934). Once the parties operate under a contract for a specific duration, the employment at-will rule is no longer applicable. See

also *Hunter v. Wehr Constructors, Inc.*, 875 S.W.2d 899 (Ky. App. 1993) (an offer to employ plaintiff for a project that mentioned the project's duration creates a jury question as to whether acceptance of the offer created a contract for a definite term).

Employers should also be aware that oral representations can modify an at-will employment relationship. In *Audiovox Corp. v. Moody*, 737 S.W.2d 468 (Ky.App. 1987), the plaintiff was an at-will office manager for the defendant. She came to believe that her supervisor was diverting company funds to his own use and benefit. When the company's management became suspicious of the plaintiff's books and began to inquire about them, she responded that she was fearful of saying anything because her supervisor would terminate her. The plaintiff testified that management assured her that if she would divulge what she knew she would not be discharged. Management then performed an audit of the company's books, but found no discrepancies. Plaintiff's supervisor summoned her into his office and asked what she had told management. When she pretended to be ignorant on the subject, her supervisor discharged her. She sued, alleging that an oral contract modifying the at-will employment relationship had been created. Audiovox defended by relying on the statute of frauds, claiming that, even if a contract had been created, it was not capable of being performed within one year. The court disagreed, holding that Audiovox could have performed the contract by intervening on the plaintiff's behalf when her supervisor discharged her. Instead, the company chose to breach its oral contract with the plaintiff. The company's reliance on the statute of frauds was held to be inapplicable, and the at-will relationship was modified by the company's oral assurances.

Employers and employees who agree to a probationary period of employment may unwittingly alter the at-will nature of their relationship. In *Norris v. Filson Care Home, Ltd.*, 1990 WL 393903 (Ky.App. 1990), the plaintiff filled out a one-page application for employment

indicating that her employment was “at-will.” She was also issued an employee handbook which stated that new employees were subject to a three-month probationary period, during which period they could be terminated for any reason at all. The handbook also contained a list of offenses for which the employee could be terminated. The handbook stated that “If an employee is to be discharged for unsatisfactory service after the three-month period is completed, a warning notice will be given and placed in the employees’ file.... Three warnings within a 12-month period of time will be grounds for dismissal.”

The plaintiff was dismissed after 90 days without receiving any warning notices. She sued for wrongful discharge. The trial court granted a directed verdict for the employer, but the Kentucky Court of Appeals reversed. According to the Court of Appeals, in a true employment at-will relationship, a probationary period is unnecessary. If the employment is truly at-will, the relationship may be terminated at any time for any reason. Thus, the court concluded that the employer must have intended something other than employment at-will when it drafted the above provisions of its employee handbook. The court found it especially relevant that the employee handbook did not contain a disclaimer that it was not intended to be a contract, or that the plaintiff’s employment was at-will.

Recently, the Kentucky Supreme Court supported employees who argued that the at-will nature of their employment relationship was undermined by the employer’s alleged fraud. In *United Parcel Service Co. v. Rickert*, 996 S.W.2d 464 (Ky. 1999), the employee established an alleged fraudulent failure to hire despite the existence of an at-will employment relationship.

UPS formerly contracted its air delivery service to several subcontractors. In the mid-1980s, UPS decided to take its air delivery service in-house. Rickert was a pilot for one of these contract air carriers. According to Rickert, **someone** from UPS told him that, so long as he

remained in his contract carrier position until the transition was complete, he would have a job at UPS. Rickert was unable to establish who made this “promise,” but this fact did not trouble the majority.

When Rickert did not obtain a job for UPS, he filed suit. UPS argued that, even if the promise was made as Rickert alleged, it was of insufficient specificity to support an action for fraud. Kentucky law demands “clear and convincing” evidence of fraud. *Wahba v. Don Corlett Motors, Inc.*, 573 S.W.2d 357, 359 (Ky. App. 1978). As the dissent pointed out, Rickert failed as a matter of law to establish an oral contract because, as Rickert testified, “UPS merely offered him a ‘chance’ of employment if he chose to remain with his contract carrier....” (*UPS* at 471.)

If Rickert were to succeed on his fraud claim, UPS argued that he would transform the alleged indefinite “promise” for employment into a guaranteed contract of employment for life. UPS argued that the trial court impermissibly allowed the jury to award Rickert damages for an 18-year employment contract. After all, at most, Rickert would have been an at-will employee of UPS if he had been hired.

The Kentucky Supreme Court rejected UPS’ argument and held that Rickert established the six elements of fraud by clear and convincing evidence, *i.e.*, (1) material representation (2) which is false (3) that was known to be false or made recklessly (4) made with inducement to be acted upon (5) acted in reliance thereon and (6) causing injury. *Rickert*, 996 S.W.2d at 468. Since UPS never came through on its alleged promise to hire Rickert, the Kentucky Supreme Court held that a verdict in his favor on the fraud count was supportable. Rickert could not prove that UPS did not intend to hire him individually, but he introduced circumstantial evidence that UPS did not intend to hire all of the contract carrier pilots. According to the court, this was “clear and convincing evidence” sufficient to maintain Rickert’s fraud action. Rickert

established detrimental reliance by showing that he forewent any job search during the transition period, while he thought he had a guaranteed job at UPS. All this "proof," the Supreme Court believed, when combined, supported a jury verdict in favor of Rickert.

WHERE ARE WE GOING?

The future of the employment at-will doctrine is uncertain. As the *Rickert* case demonstrates, the courts are more than willing to carve out exceptions to the rule when it suits the circumstances of the case. Rickert was not even able to identify the person who allegedly made the fraudulent promise to him, yet the court allowed him to maintain a fraud claim and circumvent the at-will employment rule. The court effectively transformed a promise to an applicant that he would have a job into a guaranteed contract of employment for life. Presumably, under the at-will employment rule, if Rickert had actually been hired by UPS, the company could have terminated him the day after hiring him. After all, employers do not owe a duty of good faith to their employees. *Wyant v. SCM, supra*. Nevertheless, the *Rickert* decision shows just how uneasy the courts are with the at-will employment rule. It remains to be seen how far the courts will go to undermine the rule.

The courts are also beginning to whittle away at the employment at-will rule by relying on employee handbooks. More and more often, if an employee is given a handbook or a set of policies by which he or she must abide, the employee will no longer be considered to be terminable at-will. Perhaps the most shocking example of this shift in philosophy can be found in a recent Arizona case, *Demasse v. ITT Corporation*, 1999 WL 326407 (Az. 1999), where the Arizona Supreme Court examined an employee handbook containing a policy concerning layoff. The policy stated that employees would not be laid off ahead of less-senior employees. The employer thereafter sought to change its policy, under a clause in the handbook reserving the

right to amend, modify or cancel the handbook policies unilaterally. The employer wished layoffs to be based on each employee's abilities, rather than seniority. The Arizona Supreme Court held that this unilateral change was impermissible. According to the court, once an employee relies upon provisions of the handbook, despite a disclaimer noting that the handbook was not a guarantee of continued employment, the employee may legitimately expect that the policies would not be changed during his tenure of employment. The handbook may be changed for new employees, but those changes may not be applied to current employees. In many states, continued employment would be sufficient consideration to modify the handbook, but the Arizona Supreme Court rejected this argument. If an employer in Arizona wants to change a handbook provision for existing employees, it must provide additional consideration beyond continued employment.

The Court in *Demasse* also faced an issue of whether an employee must exhaust the complaint procedure specified in an employee handbook prior to bringing suit for breach of contract. Although the same court stated that the employer was bound to follow the provisions of the employee handbook, it held that an employee is not required to exhaust the complaint procedures found therein. These two separate holdings cannot be reconciled. If the employer is bound to follow the terms of the employee handbook, since it is construed by the court to be a contract, then the doctrine of mutuality should require that an employee also be required to follow the terms of the employee handbook. The fact that the Arizona Supreme Court held that only the employer was bound to follow the provisions of the employee handbook demonstrates how far some courts are willing to go to undermine an employer's right to terminate an employee at-will.⁵

⁵ As of this date, the *Demasse* decision has not been followed by any other jurisdiction.

Many employers sense they can no longer count on judicial support for their business decisions to discharge at-will employees. To protect themselves, and in light of the U. S. Supreme Court's recent holding in *Circuit City Stores, Inc. v. Adams*, 121 S.Ct. 1302 (2001), which upheld application of the Federal Arbitration Act to employees not directly involved in interstate commerce, many employers are requiring employees to resolve disputes through arbitration. These employers reason that, if most employment is no longer at-will, then resolving employment disputes should at least be done in the cheapest and quickest manner possible.

Regardless of the direction that employment at-will takes in the future, it is clear the doctrine no longer has the vitality it once enjoyed. Courts have gone along with employees' efforts to dilute the doctrine over the past several years. Perhaps the law will come full circle, returning to a statutorily imposed minimum guarantee of employment, similar to the Statute of Artificers or the Statute of Labourers.

**ETHICAL CONSIDERATIONS FOR THE
EMPLOYMENT LAW PRACTITIONER**

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SECTION I



**ETHICAL CONSIDERATIONS FOR THE
EMPLOYMENT LAW PRACTITIONER**

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An employment law practitioner faces ethical issues each day of his or her practice. I have addressed in this paper a number of issues which one may confront in every day practice. I will supplement this paper with a power point presentation and copies of the same will be available at the seminar.

Further, no paper can be exhaustive on this issue. One should always consult the Supreme Court Rules for guidance in this area.

A. CONTACTING CURRENT AND FORMER EMPLOYEES OF AN ADVERSE PARTY.

1. Current Employees.

"In representing a client, a lawyer shall not communicate about the subject of the representation with a party the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized by law to do so." SCR 3.130(4.2). With regard to an organization, this Supreme Court Rule prohibits communication by a lawyer from one party concerning the matter in question with persons with managerial responsibility on behalf of the organization, any other person whose act or omission in connection with the matter may be imputed to the organization for purposes of civil or criminal liability, or any other person whose statement may constitute an admission on the part of the organization. SCR 3.130(4.2), cmt. 2. In regard to communications with non-managerial employees of the organization, the lawyer should disclose his identity and the fact that he is a lawyer representing a party with a claim against the organization. *Id.* See also, SCR 3.130(4.3). If, however, the non-managerial party or agent is represented in the matter by his own counsel, the lawyer may acquire that counsel's consent. *Id.*

The Kentucky Supreme Court has held that SCR 3.130(4.2)'s prohibition against contacting represented parties applies prior to the initiation of formal proceedings as well as after the initiation of such

proceedings, when those contacts concern the matter on which the party is represented. *Shoney's, Inc. v. Lewis*, Ky., 875 S.W.2d 514, 516 (1994) citing KBA E-65. In *Shoney's*, plaintiff's counsel, after being notified that the defendant was represented by counsel, met with and procured sworn statements from two employees, a general manager and a relief manager, without consent from or notice to defendant's counsel. *Shoney's, supra*, 875 S.W.2d at 514-15. In response, defendant's counsel sought disqualification of plaintiff's counsel as well as suppression of the sworn statements. *Id.* at 515. The Court, after reviewing the trial court's record, found that plaintiff's counsel admitted to taking written statements from two senior managerial employees without consent or notice. Plaintiff's counsel also admitted to taking a "stack" of written statements from other employees, and said that the statements obtained were "very important... super important" to his case. *Id.*

The Court held that there was no doubt that the statements procured were about the subject of the representation as prohibited in SCR 3.130(4.2). *Shoney's, supra*, 875 S.W.2d at 515. The Court concluded that the portion of Comment 2 to SCR 3.130(4.2), relating to managerial employees of the organization, covered the communications between plaintiff's counsel and the senior managerial employees of the defendant. *Id.* Finally, the Court held that plaintiff's counsel was disqualified, and the statements obtained were suppressed. *Id.* at 516-17.

2. Former Employees.

"The prohibition of Rule 4.2 with respect to contacts by a lawyer with employees of an opposing corporate party does not extend to former employees of that party." ABA Formal Op. 91-359. The Kentucky Bar Association ("KBA"), relying on ABA Formal Opinion 91-359, has reached the same conclusion. KBA E-381. In the KBA opinion, the committee noted that a former employee is no longer subject to the control of the organization nor in a position to speak for the organization, and therefore cannot make vicarious admissions under state and federal rules of evidence. *Id.*

The KBA committee recognized that persuasive arguments can and have been made to extend the ambit of Model Rule 4.2 to cover some former corporate employees. The committee, however, also recognized that the text of Rule 4.2 does not extend to cover former employees, nor does the comment give basis for concluding that such coverage was intended. *Id.* The committee opined that a lawyer, representing a client in a matter adverse to a corporate party represented by counsel, may communicate about the subject of the representation with an unrepresented former employee of the corporate party without the consent of the corporation's lawyer, and not violate Rule 4.2. *Id.* The committee does, however, caution lawyers not to seek or induce the former employee to violate the privilege attaching to the attorney-client communications between the former employee and the former employer's counsel to the

extent the communications are protected by the privilege, as such an attempt would violate Rule 4.4. *Id.* The committee also requires the lawyer contacting a former employee of an opposing corporate party to inform the former employee of the nature of the lawyer's role in the matter giving to the contact. *Id.* The lawyer should also disclose who the lawyer's client is and the fact that the former employer is an adverse party. *Id.* The KBA opinion also states that if the lawyer contacts a former employee who is personally represented by counsel in the matter in question, the lawyer must contact the former employee's counsel to seek consent or provide notice that the former employee will be contacted. KBA E-381.

The Kentucky Supreme Court's decision in *Humco, Inc. v. Noble* is directly on point. *See Humco, Inc. v. Noble, Ky., 31 S.W.3d 916 (2000).* One of the issues addressed in *Humco* was whether the plaintiff's lawyer violated Model Rule 4.2 by contacting ten former employees of the defendant without notice to or consent of defendant's counsel. These former employees included individuals from both management and non-management level positions. Two of the former employees were involved in meetings and discussions regarding the discipline and ultimate termination of the plaintiff's employment. The defendant brought this case before the Kentucky Supreme Court, challenging the trial court and Court of Appeals decisions not to disqualify plaintiff's counsel for communicating with the former employees without notice or consent.

The Court, citing KBA E-381 and ABA Formal Opinion 91-359, held that Model Rule 4.2 does not apply to former employees, including situations where the former employees held managerial positions or their conduct might have been the basis for imputing liability to the employer or their statements could be admitted in evidence as an admission by the employer. The Court further held that the purpose of Rule 4.2 was not to prevent the flow of information to the parties, but rather to preserve the adversarial system and prevent interference with the attorney-client privilege. The Court concluded that former employees who no longer have a present relationship with the organizational party are not parties under Rule 4.2, and thus not adverse in the litigation sense.

B. REPRESENTATION ISSUES - CONFLICTS OF INTEREST.

1. Representation of Multiple Clients - Defendants.

Supreme Court Rule 3.130(1.7) provides the general rule on conflicts of interest in representation. The Rule provides as follows:

- (a) A lawyer shall not represent a client if the representation of that client will be directly adverse to another client, unless:
 - (1) The lawyer reasonably believes the representation will not adversely affect the relationship with the other client; and
 - (2) Each client consents after consultation.

- (b) A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:
 - (1) The lawyer reasonably believes the representation will not be adversely affected; and
 - (2) The client consents after consultation. When representation of multiple clients in a single matter is undertaken, the consultation shall include explanation of the implications of the common representation and the advantages and risks involved.

An employment law practitioner faces this issue often in the context of the simultaneous representation of potentially adverse clients - the corporation and the individual supervisor.

There does not appear to be any absolute rule against representing multiple parties in litigation. Rather, the issue is decided on a case by case basis. Pursuant to Supreme Court Rule 3.130, clients may consent to such

representation after a full explanation of the advantages and risks involved in multiple representation. Comment 6 to this rule provides as follows:

[6] Paragraph (a) prohibits representation of opposing partisan litigation. Simultaneous representation of parties whose interests in litigation may conflict, such as co-plaintiff or co-defendants, is governed by paragraph (b). An impermissible conflict may exist by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of the claims or liabilities in question... On the other hand, common representation of persons having similar interests is proper if the risk of adverse effect is minimal and the requirements of paragraph (b) are met.

In representing the corporate employer and the individually named defendant employee, an employment lawyer may be faced with a conflict of interest too substantial to overcome. In certain cases, the company, to avoid legal liability, must show that the employee in question was acting outside the scope of his job. The employee, on the other hand, has an interest in establishing he acted within the scope of his duties, especially where such a finding might entitle him to indemnity from the corporate employer. If, however, the corporation acknowledges that the employee was acting within the scope of his duties, no conflict exists and multiple representation is not inappropriate.

The District of Columbia Bar has actually adopted a test for determining the propriety of joint representation of potentially adverse parties. The test is based on ABA Committee on Ethics and Professional Responsibility, Informal Opinion 1441. It consists of the following:

- (1) The co-parties agree to a single comprehensive statement of facts describing the occurrence.
- (2) The attorney reviews the statement of facts from the perspective of each of the parties and determines that it does not support a claim by one against the other.
- (3) The attorney determines that no additional facts are known by each party which might give rise to an independent basis of liability against the other or against themselves by the other.
- (4) The attorney advises each party as to the possible theories of recovery or defense which may be foregoing through this joint representation based on the disclosed facts. DR 5-105(C).
- (5) Each party agrees to forego any claim or defense against the other based on the facts known by each at the time. DR 5-105(C).
- (6) Each party agrees that the attorney is free to disclose to the other party, at the attorney's discretion, all facts obtained by the attorney.
- (7) The attorney outlines potential pitfalls in multiple representation, and advises each party of the opportunity to seek the opinion of independent counsel as to the advisability of the proposed multiple representation; and, each either consults separate counsel or advises that no separate consideration is desired.
- (8) Each party acknowledges that the facts not mentioned now but later discovered may reveal differing interests, which, if they do not compromise these differences, may require the attorney to withdraw from the representation of both without injuring either. DR 2-110; 5-101(B).
- (9) Each party agrees that the attorney may represent both in the litigation. DR 5-105(C).

2. **Representation of Multiple Clients - Plaintiffs.**

Defense counsel is not alone in this legal quandary. Plaintiff counsel must insure that the joint representation of multiple plaintiffs does not violate this Supreme Court Rule. For example, in a discharge context, one plaintiff could claim that the other alone committed the offense for which they were both discharged. In addition, pursuant to Comment 6, counsel must look to the parties' testimony and determine if there is substantial discrepancy as well as determine whether there are substantial different possibilities of settlement.

C. PAYMENT OF LAWYER'S SERVICES.

Defense counsel often run into this issue when they are representing the supervisory employee and the corporate defendant is paying the attorneys' fee for the supervisory employee. Comment 9 to Supreme Court Rule 3.130 addresses this issue. The comment states as follows:

[9] A lawyer may be paid from a source other than the client, if the client is informed of that fact and consents and the arrangement does not compromise the lawyer's duty of loyalty to the client. See Rule 1.8(f). For example, when an insurer and its insured have conflicting interests in a matter arising from a liability insurance agreement, and the insurer is required to provide special counsel for the insured, the arrangement should assure the special counsel's professional independence. So also, when a corporation and its directors or employees are involved in a controversy in which they have conflicting interests, the corporation may provide funds for separate legal representation of the directors or employees, if the clients consent after consultation and the arrangement ensures the lawyer's professional independence.

D. POSITIONAL CONFLICTS.

Although I represent employers 95% of the time, I do take plaintiff cases. As such, I am aware of the potential conflict of interest in this area. Conflict can occur in this area when advocacy of a legal issue on behalf of one client could adversely affect a client in a second matter through precedential effect.

Although neither the Code nor the Model Rules prohibit most positional conflicts, both include provisions that could encompass some of the matters. If any representation would involve misuse of client confidences, it would be prohibited. In addition, if accepting representation would compromise a lawyer's "independent professional judgment," or would "adversely affect" the lawyer-client relationship, it would be prohibited. See Supreme Court Rules 3.130(1.6) and (1.7).

There are three comments to Supreme Court Rule 3.130(1.7) which address loyalty. They are as follows:

[1] Loyalty is an essential element in the lawyer's relationship to a client. An impermissible conflict of interest may exist before representation is undertaken, in which event the representation should be declined. If such a conflict arises after representation has been undertaken, the lawyer should withdraw from the representation. *See Rule 1.16.* Where more than one client is involved and the lawyer withdraws because a conflict arises after representation, whether the lawyer may continue to represent any of the clients is determined by Rule 1.9. *See also Rule 2.2(c).* As to whether a client-lawyer relationship exists or, having once been established, is continuing, see Comment to Rule 1.3 and Scope.

[2] As a general proposition, loyalty to a client prohibits undertaking representation directly adverse to that client without that client's consent. Paragraph (a) expresses that general rule. Thus, a lawyer ordinarily may not act as advocate against a person the lawyer represents in some other matter, even if it is wholly unrelated. On the other hand, simultaneous representation in unrelated matters of clients whose interests are only generally adverse, such as competing economic enterprises, does not require consent of the respective clients. Paragraph (a) applies only when the representation of one client would be directly adverse to the other.

[3] Loyalty to a client is also impaired when a lawyer cannot consider, recommend or carry out an appropriate course of action for the client because of the lawyer's other responsibilities or interests. The conflict in effect forecloses alternatives that would otherwise be available to the client. Paragraph (b) addresses such situations. A possible conflict does not itself preclude the representation. The critical questions are the likelihood that a conflict will eventuate and, if it does, whether it will materially interfere with the lawyer's independent professional judgment in considering alternatives or foreclose courses of action that reasonably should be pursued on behalf of the client. Consideration should be given to whether the client wishes to accommodate the other interest involved.

See also ABA Formal Ethics Opinion 93-377 (Oct. 16, 1993)

(when a lawyer is asked to advocate a position with respect to a substantive legal issue that is directly contrary to the position being urged on behalf of another client in a different and unrelated matter which is being litigated in the same jurisdiction, the lawyer, in the absence of informed consent by both clients, should refuse to accept the second representation if there is a substantial risk that the lawyer's advocacy on behalf of one client will create a legal precedent which is likely to materially undercut the legal position being urged on behalf of the other client).

E. CONFLICT OF INTEREST - FORMER CLIENT.

Supreme Court Rule 3.130(9) provides as follows:

A lawyer who has formerly represented a client in a matter shall not thereafter.

- (a) Represent another person in the same or a substantially related matter in which that person's interests are materially adverse to the interests of the former client unless the former client consents after consultation.
- (b) Represent a person in the same or a substantially related matter in which a firm with which the lawyer formerly was associated had previously represented a client
 - (1) whose interests are materially adverse to that person; and
 - (2) about whom the lawyer had acquired information protected by Rules 1.6 and 1.9(c) that is material to the matter; unless the former client consents after consultation.
- (c) A lawyer who has formerly represented a client in a matter of whose present or former firm has formerly represented a client in a matter shall not thereafter:
 - (1) Use information relating to the representation to the disadvantage of the former client except as Rule 1.6 or Rule 3.3 would permit or require with respect to a client or when the information has become generally known; or
 - (2) Reveal information relating to the representation except as Rule 1.6 or Rule 3.3 would permit or require with respect to a client.

F. INSURANCE ISSUES.

In an increasing number of cases, employers and individual defendants have been successful in establishing insurance coverage for employment law claims made against them. In other cases, insurers will provide defense costs (and sometimes actually retain counsel to represent the insured) under a reservation of rights. In such cases, attorneys must be aware of the potential conflicts between the interests of the insurer and the insured. It has been made clear that the rules of professional conduct, and not the insurance contract, govern the ethical obligations of a lawyer retained by the insurer to defend its insured.

Formal Opinion 96-403 imposes special requirements on lawyers defending an insured under an insurance policy that permits the insurer to control the defense and settle within policy limits in its sole discretion. The Opinion requires the lawyer to communicate to the insured the limitations that the policy places on his representation, "preferably early in the representation." Once the lawyer has so informed the insured, he need not consult the insured again before settling at the direction of the insured.

G. MISCELLANEOUS ISSUES.

1. Attorney-client Privilege Does Not Cover Preparing Former Employee for Deposition.

The attorney-client privilege does not shield communications between a corporation's in-house lawyers and a non-client former employee about the latter's upcoming deposition testimony, the U.S. District Court for the Southern District of New York has held. (*New York City v. Coastal Oil New York, Inc.*, S.D.N.Y., No. 96 Civ. 8667 (RPP), 2/7/00).

Judge Robert P. Patterson Jr. decided that a corporation's opponent in litigation would be permitted to inquire about witness preparation sessions in which inside corporate counsel prepared a former employee for an impending deposition. The former employee did not view the lawyers as his attorneys, and they were not investigating allegations against the corporation, Patterson explained.

At the deposition of a former employee of Coastal Oil, he was asked about earlier conversations with two in-house lawyers for the corporate defendants. The employee acknowledged that he had spoken with the two lawyers in preparation for the deposition. However, he was directed by his lawyer - the corporate defendants' outside counsel - not to answer questions about the preparation that he received from the in-house lawyers. The conversations in question were protected by the attorney-client privilege, the defendants argued.

The Court distinguished Upjohn Co. v. United States, 449 U.S. 383 (1981), in which a corporate defendant was held entitled to the protection of the lawyer-client privilege with respect to the conversations of in-house counsel with corporate employees while investigating allegations against the corporation.

The present case, in contrast, involved a discovery dispute in which the plaintiffs were seeking to find out whether a third party witness had his memory "refreshed" by in-house counsel. The allegations against the corporate defendants had long since been investigated and had been the subject of a criminal trial, he noted, and there was no showing that the in-house lawyers were acting in an investigatory capacity during the conversations in question.

More on point, the Court noted, was Peralta v. Cendant Corp., 190 F.R.D. 38 (D. Conn. 1999), which allowed limited discovery of a former employee's conversations with counsel for the defendant. Patterson also cited the Restatement of the Law Governing Lawyers Section 123, Comment e (Proposed Final Draft No 1, 1996), which states that for the corporate privilege to apply a former employee must have "an agency relationship to the principal-organization at the time of the communication."

The Court did limit the questioning to the in-house lawyers' activities that aided in preparing to be deposed, such as information the employee provided to him during the conversations, actions and

statements that "refreshed" his recollection, reminders of his prior testimony or prior statements, references to the testimony of other witnesses, or any instructions about his testimony that he received from the in-house lawyers.

2. **Lawsuits by Former In-house Attorneys.**

There has been a plethora of cases discussing whether or not former in-house attorneys have standing to bring claims against their former employers. The ABA Ethics Committee has held that there is nothing in the Model Rules that precludes a lawyer from suing his or her former client. In Opinion 01-424, rendered in September 2001, the Committee okayed such a lawsuit, but also guarded against the disclosure of unnecessary information.

3. **Secretly Recording Conversations.**

On June 24, 2001, the ABA Ethics Committee abandoned its longstanding view that a lawyer may not ethically record a conversation with the consent of all parties and advised instead that a lawyer does not violate the Model Rules by secretly, but lawfully, taping a conversation. Formal Opinion 01-422.

4. Candor Toward the Court.

Supreme Court Rule 3.130(3.3) provides as follows:

- (a) A lawyer shall not knowingly:
 - (1) Make false statement of material fact or law to a tribunal;
 - (2) Fail to disclose a material fact to the tribunal when disclosure is necessary to avoid a fraud being perpetrated upon the tribunal;
 - (3) Offer evidence that the lawyer knows to be false. If a lawyer has offered material evidence and comes to know of its falsity, the lawyer shall take reasonable remedial measures.
- (b) The duties stated in paragraph (a) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6
- (c) A lawyer may refuse to offer evidence that the lawyer reasonably believes is false.
- (d) In an ex parte proceeding, a lawyer shall inform the tribunal of all material facts known to the lawyer which will enable the tribunal to make an informed decision, whether or not the facts are adverse.
- (e) The obligation of the advocate under these rules is subordinate to such constitutional requirements as may be announced by the courts.

[Adopted by Order 89-1, eff. 1-1-90]

5. Fairness.

Supreme Court Rule provides as follows:

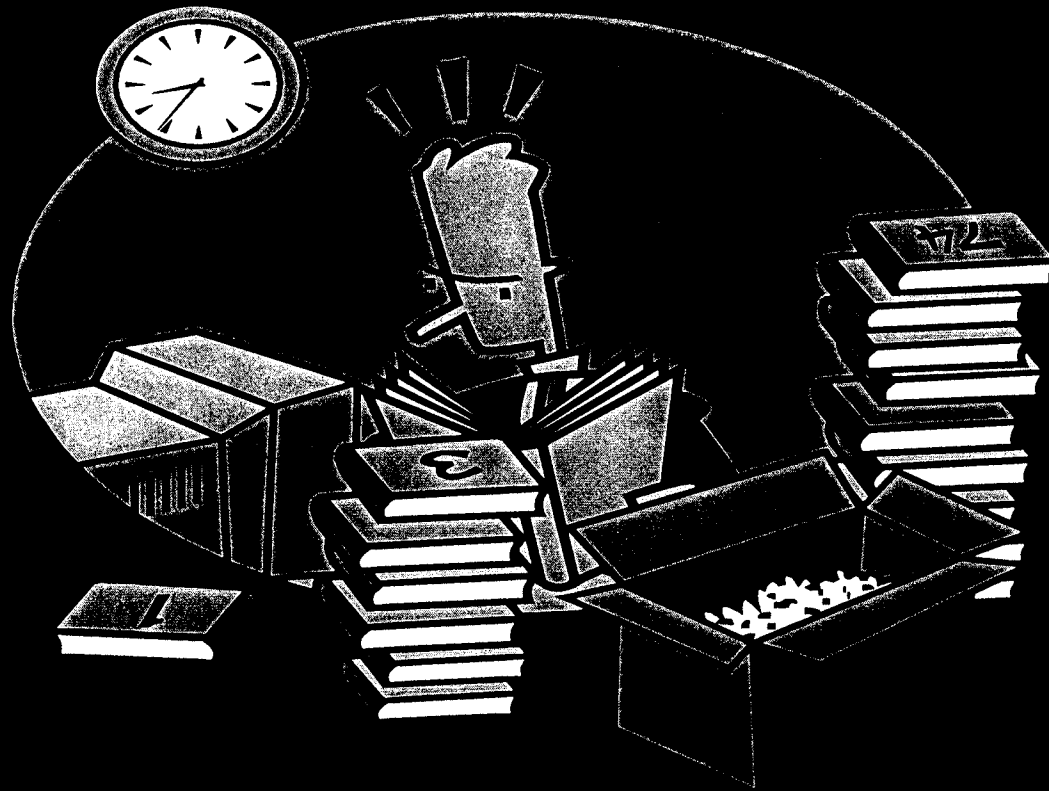
A lawyer shall not:

- (a) Unlawfully obstruct another party's access to evidence or unlawfully alter, destroy or conceal a document or other material having potential evidentiary value. A lawyer shall not counsel or assist another person to do any such act;
- (b) Knowingly or intentionally falsify evidence, counsel or assist a witness to testify falsely, or offer an inducement to a witness that is prohibited by law;
- (c) Knowingly or intentionally disobey an obligation under the rules of a tribunal except for an open refusal based on an assertion that no valid obligations exists;
- (d) In pretrial procedure, knowingly or intentionally make a frivolous discovery request or deliberately fail to make reasonably diligent effort to comply with a legally proper discovery request by an opposing party;
- (e) In trial, knowingly or intentionally allude to any matter that the lawyer does not reasonably believe is relevant or that will not be supported by admissible evidence, assert personal knowledge of facts in issue except when testifying as a witness, or state a personal opinion as to the justness of a cause, the credibility of a witness, the culpability of a civil litigant or the guilt or innocence of an accused; or
- (f) Present, participate in presenting, or threaten to present criminal or disciplinary charges solely to obtain an advantage in any civil or criminal matter.

[Adopted by Order 89-1, eff. 1-1-90]



Ethical Issues for the Employment Law Attorney





Ethics

- Belief
- Conduct
- Honesty
- Ideal
- Integrity
- Morality
- Principles
- Right and Wrong

(Roget's 21st Century Thesaurus)

Can You Identify An Ethical Problem?

- 1) Representation of two individuals (plaintiffs) suing an employer
- 2) Payment of attorneys' fees by employer for individual supervisor
- 3) Having a bologna sandwich for lunch instead of a chicken salad sandwich
- 4) Contacting a former employee of a company your client is suing
- 5) Representation of employers (defendants) and employees (plaintiffs) in different lawsuits

Multiple Representation Issues



Defendants: Corporation/Supervisor

- Sexual Harassment Case

- Law
- Acting within corporate capacity
- Denied during investigation, but admits to you after “grilling” deposition

- Assault and Battery Case

- Law
- Acting within corporate capacity

Multiple Representation Issues

Plaintiffs: Two Employees Making A Claim
Against Employer

- Testimony differs between plaintiffs
- Testimony differs between witnesses
- Settlement differences

Multiple Representation Issues

- Supreme Court Rule 3.130 (1.7) paragraph b (page 7 of outline)
- Believe representation will not be adversely affected
- Clients consent after consultation
- Consultation: implications of common representation
 - advantages
 - disadvantages/risks
- Set forth in letter to both parties

Multiple Representation Issues

Considerations

- Testimony of parties
- Testimony of witnesses
- Settlement possibilities
- Liability issues
- Position as to opposing party

Payment of Fees



Payment of Fees

Defendants: Corporation/Supervisory
Employee

- Company is paying for employee's lawyer
- Supreme Court Rule 3.130 (1.7) paragraph 9
 - 1) Client must be informed (deposition testimony experience)
 - 2) Client must consent (include in letter to clients)
 - 3) Arrangement does not compromise the lawyer's duty of loyalty to the client (who do you represent) (if company is paying, will your decision-making be affected)

Tape Recording Conversations



Tape Recordings

- June 24, 2001 ABA Ethics Committee Decision
(Formal Opinion 01-422, 6/24/01)
(ABA Standing Comm. on Ethics and Professional Responsibility)
- Old rule: A lawyer may not ethically record a conversation without the consent of all parties (Opinion 337-1974)

Tape Recordings

- New Rule:
 - a) a lawyer may secretly tape record a conversation with a third person
 - b) “the mere act of secretly but lawfully recording a conversation inherently is not deceitful”
 - c) a lawyer may not falsely deny that a conversation is being recorded
 - d) a lawyer may not secretly record a conversation in a state that forbids such, without all parties’ consent

Tape Recordings

Taping A Client

- a) Committee members divided on the question of secretly recording a client, but agreed that it was inadvisable to do so
- b) Clients must assume a lawyer is memorializing, in some way, their communications
- c) Electronic recording can save time and trouble and ensures accuracy
- d) Discovery of such would undermine trust/confidence; therefore even if not unethical, inadvisable except in circumstances 1) where lawyer has no reason to believe client would object or 2) where exceptional circumstances exist
- e) Exceptional Circumstances: criminal act

Tape Recordings

- Debose-Parent v. Hyatt, E.D. La., No. 00-3795, 6/21/01
- Employer's Attorney ex-parte communications with represented plaintiff about claim
- Employee (on advice of counsel) secretly recorded her conversation with defense attorney
- Formal bar complaint filed
- Lawsuit filed by defense attorney claiming violation of federal wiretapping law
- Lawsuit dismissed - consensual interception exception applied

Electronic Issues

(Cell Phones, Fax Machines, E-Mail)



Cellular Telephones

- Confidentiality Issues
- Public airwaves v. telephone lines
- Conversations can be intentionally intercepted by sophisticated scanners
- Some bar ethics opinions have warned attorneys to not use cellular telephones to discuss cases unless the client is informed and consents (N.Y., N.C., Mass., N.H., IA, Ill., Wash., Cal.)
- Also be aware client may be speaking to you over cellular telephone

E-Mail Communications

- Confidentiality
- Security
- Susceptible to interception to anyone with computer access to which a lawyer “logs on” (simple passwords)
- Early opinions concluded confidential communications with clients should not occur over the internet without “encryption” or unless the client consents to “non-secure” communications
- Later opinions have backed off this stance unless “unusual circumstances” exist which require enhanced security measures
- Expectation for privacy in e-mail is no less than in a telephone call
- Kentucky Bar Ethics Committee Advisory Opinion E-403 (1998)

Inadvertent Disclosure or Interception of Communications

Cellular Telephones - Digital, not analog

Letters, E-Mails - “Privileged and Confidential:
Attorney-Client Communication”

Telecopy and E-Mail Transmissions -

Confidentiality Notice: This message is intended only for the addressee and may contain information that is privileged, confidential and/or attorney work product. If you are not the intended recipient, do not read, copy, retain or disseminate this message or any attachment. If you have received this message in error, please call the sender immediately at xxx-xxx-xxxx and delete all copies of this message and any attachment. Neither this transmission of this message or any attachment, nor any error in transmission or misdelivery shall constitute a waiver of any applicable legal privilege.

Lawsuits by Former In-House Attorneys



In-House Attorneys

Can an In-House Attorney Ethically Sue His or Her Former Employer?

ABA Standing Committee on Ethics and Professional Responsibility, Formal Opinion 01-424 (9/22/01)

- * Not unethical to pursue a wrongful discharge action against ex-client (employer) so long as lawyer does not reveal more client information than reasonably necessary to establish the claim and takes affirmative steps to avoid unnecessary disclosure and limit the information revealed

In-House Attorneys

- Supreme Court Rule 3.130 (1.9) forbids revealing of information relating to representation or to use such information to former client's disadvantage
- Supreme Court Rule 3.130 (1.6) creates an exception and allows information to be revealed to the extent lawyer reasonably believes necessary to establish a claim on behalf of the lawyer in a controversy between the lawyer and the client
- Affirmative Steps to Prevent Disclosure of Information
 - 1) in camera review at pre-trial evidentiary hearing
 - 2) sealing the record of the proceedings
 - 3) not disclosing the parties' names

Supreme Court Rule 3.130 (1.6) comments 18,19.

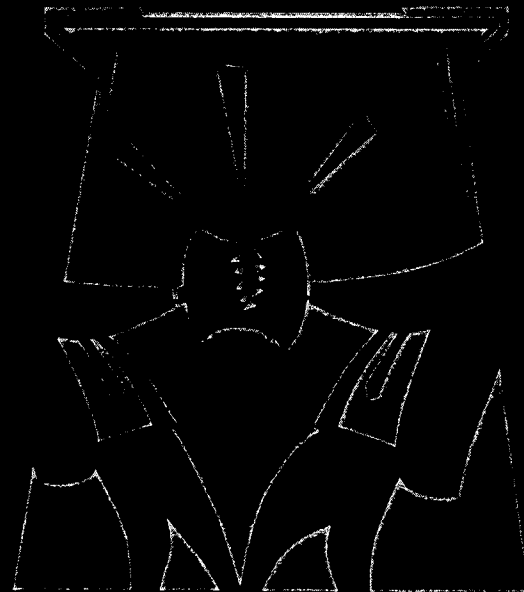
In-House Attorneys

Is there such an animal as a retaliatory discharge claim by an in-house counsel against her/his employer (former client)?

Three approaches:

- 1) breach of implied contract
- 2) retaliatory discharge claims allowed if claim can be proven without violation of obligation to respect client confidences
- 3) deny claims for retaliatory discharge

Positional Conflicts



- Represent Employers 90% of time
- Take 5-6 Plaintiff Cases a Year
- ABA Formal Ethics Opinion 93-377 (1993)
 - 1) Is there substantial risk that the lawyer's advocacy on behalf of one client will create a legal precedent which is likely to materially undercut the other's legal position

Contacting Current and Former Employees of Adverse Party



Contacting Current Employees of Adverse Party

- Supreme Court Rule 3.130 (4.2)
- Supervisors v. Non-Managerial Employees
- Disclose identity and who he is representing

Contacting Former Employees of an Adverse Party

- ABA Formal Opinion 91-359
- KBA Ethics Opinion 381
- Humco, Inc. v. Noble, Ky., 31 S.W.3d 916
(2000)

TOP 10 REASONS AS TO
WHY YOU MAY SUSPECT
YOU HAVE COMMITTED AN
ETHICAL VIOLATION

10. You receive a certified letter from the Kentucky Bar Association Ethics Committee
9. Bill Fortune and Rick Underwood want to take you to lunch.
8. You receive a paid subscription by an anonymous individual to the “Ethics For Attorneys To Live By” journal.

7. Somewhere in the midst of your representation of your client he asks “when did you become so ethical?”
6. You notice the deposition of the President of the Company and upon meeting him realize you interviewed him thinking he was a clerical employee.
5. During a cell phone conversation with your client, you notice opposing counsel in the parked car next to you taking notes and holding up a sign that says “keep talking.”

1. You walk into your office to find the two plaintiffs you are representing in a brawl and calling each other liars.





IN HOUSE COUNSEL

VS.

FORMER EMPLOYER



steps to ensure that the foreign lawyer is specially trained to provide advice on the laws of the foreign jurisdiction and to represent clients in its legal system. Moreover, the committee said, members of the firm must satisfy themselves that the arrangement complies with the law of the jurisdictions in which the firm practices.

For instance, the committee said, qualification as a foreign lawyer should be accorded to an *avocat* (courtroom lawyer) or *conseil juridique* (transactional or business lawyer) but not to a *notario* (notary), which is a "substantially different functionary" in most civil law jurisdictions.

If professionals in a foreign jurisdiction do not qualify as members of a recognized legal profession in their home country, the committee said, they should be considered nonlawyers for purposes of Rule 5.4 and would not be eligible for partnership.

Differing Standards. U.S. lawyers should remain aware, the committee advised, that ethics standards in a number of foreign countries—such as those governing confidentiality—differ from the standards that apply to lawyers in the United States, and that responsible lawyers in the U.S. firms should not only make certain that clients understand these differences but also ensure that client information in U.S. offices remains protected.

Finally, the committee warned that U.S. lawyers must take care not to help the foreign lawyer engage in unauthorized practice. Calling upon a foreign lawyer to provide advice on the law of a foreign jurisdiction to a client who is located in the United States ordinarily would not violate Rule 5.5, the committee said, so long as the foreign lawyer is not regularly in the jurisdiction where the U.S. office is located and the matter has a relationship to the jurisdiction in which the foreign lawyer is admitted to practice.

Corporate Counsel

Former In-House Lawyer May Pursue Claim For Wrongful Discharge, ABA Opinion Advises

It is not unethical for a former in-house corporate counsel to pursue a wrongful discharge action against her ex-client so long as the lawyer does not reveal more client information than reasonably necessary to establish the claim, the ABA's ethics committee advised Sept. 22 (ABA Standing Comm. on Ethics and Professional Responsibility, Formal Op. 01-424, 9/22/01).

The committee grounded its advice on the exception in Model Rule of Professional Conduct 1.6 that authorizes disclosure of client information when necessary to establish a "claim" in a dispute between the lawyer and the client. But a lawyer suing a former client-employer must take affirmative steps to guard against unnecessary disclosure of information learned during the representation, the opinion cautions.

The opinion does not address the underlying legal question of whether a former in-house lawyer who is fired for complying with her ethical obligations has a cause of action for retaliatory discharge—a matter on which courts have reached opposite conclusions. Nor does it address the subject of wrongful discharge claims

by law firm associates. Case law on those issues is summarized in extensive footnotes in the opinion, however.

'Claim' Against Ex-Client. "There is nothing in the Model Rules that precludes a lawyer from suing her former client and, in fact, the Rules contemplate that such actions may occur," the opinion states.

The committee acknowledged that Rule 1.9 forbids a lawyer who has formerly represented a client to reveal information relating to the representation or to use such information to the former client's disadvantage.

But that rule carves out an exception, the committee noted, for disclosure permitted by Rule 1.6, and paragraph (b)(2) of Rule 1.6 allows a lawyer to reveal client information "to the extent the lawyer reasonably believes necessary . . . to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client."

"There is nothing in the Model Rules that precludes a lawyer from suing her former client and, in fact, the Rules contemplate that such actions may occur."

ABA FORMAL OP. 01-424

The committee decided that a retaliatory discharge or similar claim by an in-house lawyer against her former employer constitutes a "claim" under the Rule 1.6(b)(2) exception. Although the Model Rules do not define "claim," the committee found that paragraph (b)(2) was intended to enlarge the predecessor Model Code of Professional Responsibility provision beyond claims for fees to reach other claims such as recovery of property from the client.

In addition, the committee relied on *Burkhart v. Semitool Inc.*, 5 P.3d 1031 (Mont. 2000), which held, the committee said, that Montana's identical version of Rule 1.6 permits confidential client information to be revealed by a former in-house lawyer pursuing a retaliatory discharge claim against her ex-employer.

Constraints on Disclosure. The opinion warns that in pursuing a retaliatory discharge claim, "the lawyer must limit disclosure of confidential client information to the extent reasonably possible."

The former in-house lawyer "must take reasonable affirmative steps"—which will be unique to each case—to guard against unnecessary disclosure of confidential client information, the committee said. It suggested that these specific protections be considered:

- in camera review at a pretrial evidentiary hearing;
- sealing the record of the proceedings; and
- not disclosing the parties' names.

In giving this advice, the committee drew on the comment to Rule 1.6, which states that "[a] lawyer must make every effort practicable to avoid unnecessary disclosure of information relating to a representation, to limit disclosure to those having the need to know it, and to obtain protective orders or make other arrangements limiting the risk of disclosure."

1ST ITEM of Level 1 printed in FULL format.

AMERICAN BAR ASSOCIATION STANDING COMMITTEE ON ETHICS AND PROFESSIONAL
RESPONSIBILITY

Formal Opinion 01-424

A Former In-House Lawyer May Pursue a Wrongful Discharge Claim Against Her
Former Employer and Client As Long As Client Information Properly Is Protected

September 22, 2001

The Model Rules do not prohibit a lawyer from suing her former client and employer for retaliatory discharge. In pursuing such a claim, however, the lawyer must take care not to disclose client information beyond that information the lawyer reasonably believes is necessary to establish her claim.

Retaliatory Discharge Claims

In this opinion, we address the constraints that may be imposed on retaliatory or wrongful discharge claims by in-house lawyers against their former employers and clients under the Model Rules of Professional Conduct. We note at the outset that the Committee does not address the legal question of whether the discharge of an in-house lawyer--even one that alleges that the employer has "retaliated" for the lawyer's proper adherence to her ethical obligations--gives rise to an enforceable claim. n1 The Committee only addresses the ethical considerations that arise under the Model Rules when such an action is permitted under applicable state law. n2

n1 This opinion also does not address a retaliatory discharge claim by a lawyer against the law firm by which she is employed. A retaliatory discharge claim by a former in-house lawyer may be distinguished from a wrongful discharge suit by a lawyer against a law firm. A law firm and lawyer are bound to conduct their practices in accordance with prevailing ethical obligations. *Wieder v. Skala*, 80 N.Y.2d 628, 636, 609 N.E.2d 105, 108, 593 N.Y.S.2d 752, 755 (N.Y. 1992). The employer of an in-house lawyer necessarily is not bound by legal ethical rules. See *Mourad v. Automobile Club Ins. Ass'n*, 465 N.W.2d 395, 400 (Mich. Ct. App. 1991). In *Wieder*, an associate sued a law firm claiming he was fired for insisting that the firm comply with governing disciplinary rules and that it report the misconduct of another associate. 80 N.Y.2d at 631, 609 N.E.2d at 106, 593 N.Y.S.2d at 753. The New York Court of Appeals held there was an implied obligation that both the firm and the associate would carry out the employment contract in compliance with ethical obligations, meaning the firm could not require an associate to violate ethical obligations in order to keep his job., 80 N.Y.2d at 636, 609 N.E.2d at 108, 593 N.Y.S.2d at 755.

n2 Courts permit retaliatory discharge claims by former employees as an exception to the employment-at-will doctrine, which avows that when an employee does not have a written employment contract and the term of employment is of indefinite duration, the employer can terminate the employee for "good cause, bad cause, or no cause at all." See generally *Pugh v. See's Candies, Inc.*, 116 Cal. App. 3d 311, 319-21, 171 Cal. Rptr. 917, 920-22 (1st Dist. 1981); *Brian F. Berger*, Note, Defining Public Policy Torts In At-Will Dismissals, 37 STANFORD L. REV. 153, 153 (1981). The exception provides relief to employees discharged for reasons contrary to public policy, such as for exercising statutory or

September 22, 2001

constitutional rights or for whistleblowing when an employee refuses to violate the law and reports an employer's wrongdoing. E.g., *Parker v. M & T Chemicals*, 236 N.J.Super. 451, 460, 566 A.2d 215, 220 (N.J. Super. Ct. App. Div. 1989) (court construed state whistleblower act as compelling a retaliating employer to pay damages to an employee-lawyer who is discharged wrongfully or mistreated for refusing to join a scheme to cheat a competitor or for any reason that is violative of law, fraudulent, criminal, or incompatible with a clear mandate of the state's public policy concerning public health, safety or welfare); *Perks v. Firestone Tire & Rubber Co.*, 611 F.2d 1363, 1365-66 (3d. Cir. 1979) (Pennsylvania statute forbidding employer from requiring polygraph test as condition for employment or continuation of employment embodies a recognized facet of public policy). In addition, certain states have enacted legislation in this area. For example, in Louisiana, an employment contract in restraint of membership in labor organizations is contrary to public policy. La. Rev. Stat. Ann § 823 (West 2001).

Employers faced with retaliatory discharge suits from former in-house lawyers assert an absolute right to discharge their lawyer at any time and for any reason because no client should be forced into representation by a lawyer in whom that "confidence and trust lying at the heart of a fiduciary relationship has been lost." *General Dynamics Corp. v. Superior Court*, 7 Cal.4th 1164, 1174, 876 P.2d 487, 493, 32 Cal.Rptr.2d 1, 7 (Cal. 1994); *Parker v. M & T Chemicals*, 236 N.J.Super. at 458, 566 A.2d at 219. The absolute right to terminate an in-house lawyer under any circumstances without consequence has been limited, however, by a number of courts in recent years that have noted that the in-house lawyer uniquely is bound to her client. Where outside counsel face dilemma with clients, the in-house lawyer faces "a virtually complete dependence on the good will and confidence of a single employer to provide livelihood and career success." *General Dynamics*, 7 Cal.4th at 1182, 876 P.2d at 498. 32 Cal.Rptr.2d at 12. Thus, some courts have permitted the retaliatory discharge claim by the former in-house lawyer. These courts find there are compelling reasons of public policy that make it appropriate to impose legal consequences for dismissing an in-house lawyer. Specifically, they conclude that the public has an interest in insuring that lawyers abide by their ethical obligations.

Courts also have recognized state-adopted codes of ethics for lawyers as a reflection of public policy. E.g., *Mourad v. Automobile Club*, 465 N.W.2d 395 at 400 (court refused to address in-house lawyer's retaliatory discharge claim but held that lawyer could maintain action for breach of contract based on retaliatory demotion and constructive discharge resulting from his refusal to violate code of professional conduct). In addition to *Mourad*, other courts that have provided relief to an in-house lawyer dismissed in retaliation for either insisting on adhering to mandatory ethical norms of the profession or for refusing to violate them include *GTE Products Corp. v. Stewart*, 421 Mass. 22, 29, 653 N.E.2d 161, 165 (Mass. 1995) (public interest is better served if in-house counsel's resolve to comply with ethical and statutorily mandated duties is strengthened by providing judicial recourse when an employer's demands are in direct and unequivocal conflict with those duties) and *General Dynamics Corp.*, 7 Cal.4th at 1186, 876 P.2d at 501, 32 Cal.Rptr.2d at 15 (in-house counsel should be permitted to pursue a claim for wrongful discharge if the claim is "founded on allegations that an in-house attorney was terminated for refusing to violate a mandatory ethical duty embodied in [the state's code of professional conduct]"). See also *Willy v. Coastal Corp.*, 647 F. Supp. 116, 118 (S.D. Tex. 1986), rev'd on other grounds, 855 F.2d 1160 (5th Cir. 1988)



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(implying that code of ethics reflected public policy, but holding other remedies, such as withdrawal from representation, sufficient to avoid violating public policy); *Herbster v. North American Co.*, 501 N.E.2d 343, 346-48 (Ill. App. Ct. 1986), appeal dismissed, 114 Ill.2d 545, 108 Ill. Dec. 417, 508 N.E.2d 728 (1987) (stating that code of ethics reflected public policy despite disallowing vice-president in charge of legal department's retaliatory discharge claim). On the other hand, the Illinois Supreme Court rejected a lawyer retaliatory discharge claim in *Balla v. Gambro*, 145 Ill.2d 492, 501-02, 584 N.E.2d 104, 108-09, 164 Ill. Dec. 892, 896-97 (Ill. 1991), on the grounds that public policy adequately is safeguarded without extending the tort of retaliatory discharge to in-house counsel and that permitting such suits would have an undesirable effect on the lawyer-client relationship.

The Model Rules and Retaliatory Discharge Claims

There is nothing in the Model Rules that precludes a lawyer from suing her former client and, in fact, the Rules contemplate that such actions may occur.
n3

n3 See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.6 (2001). Rule 1.6 states:

(a) A lawyer shall not reveal information relating to representation of a client unless the client consents after consultation, except for disclosures that are impliedly authorized in order to carry out the representation, and except as stated in paragraph (b).

(b) A lawyer may reveal such information to the extent the lawyer reasonably believes necessary:

(1) to prevent the client from committing a criminal act that the lawyer believes is likely to result in imminent death or substantial bodily harm; or

(2) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client.

The principal obligations of a lawyer to her former client are to continue to maintain the confidentiality of the client information learned during the course of the representation and to neither "use information relating to the representation to the disadvantage of the former client" nor "reveal information relating to the representation" n4 except, in both cases, as permitted by Rule 1.6 or Rule 3.3. n5 Under Rule 1.6(b)(2), a lawyer may reveal information relating to the representation of the client "to the extent the lawyer reasonably believes necessary . . . to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client"

n4 Rule 1.9 states in part:

(c) A lawyer who has formerly represented a client in a matter of whose present or former firm has formerly represented a client in a matter shall not thereafter:

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(1) use information relating to the representation to the disadvantage of the former client except as Rule 1.6 or Rule 3.3 would permit or require with respect to a client, or when the information has become generally known; or

(2) reveal information relating to the representation except as Rule 1.6 or Rule 3.3 would permit or require with respect to a client.

n5 Rule 3.3 states in pertinent part:

(a) A lawyer shall not knowingly:

(1) make a false statement of material fact or law to a tribunal;

(2) fail to disclose a material fact to a tribunal when disclosure is necessary to avoid assisting a criminal or fraudulent act by the client,

(3) fail to disclose to the tribunal legal authority in the controlling jurisdiction known to the lawyer to be directly adverse to the position of the client and not disclosed by opposing counsel; or

(4) offer evidence that the lawyer knows to be false. If a lawyer has offered material evidence and comes to know of its falsity, the lawyer shall take reasonable remedial measures.

(b) The duties stated in paragraph (a) continue to the conclusion of the proceeding, and apply even if compliance requires disclosure of information otherwise protected by Rule 1.6.

The term "claim" is not defined under the Model Rules. In the predecessor Code of Professional Responsibility, DR 4-101 (C) allowed a lawyer to reveal "confidences or secrets necessary to establish or collect his fee or to defend himself or his employees or associates against an accusation of wrongful conduct." n6 When the Model Rules were adopted in 1983, the Comments explained: "With regard to paragraph (b) (2), DR 4-101 (c) (4) provided that a lawyer may reveal 'confidences or secrets necessary to establish or collect his fee or to defend himself or his employers or associates against an accusation of wrongful conduct.' Paragraph (b) (2) enlarges the exception to include disclosure of information relating to claims by the lawyer other than for the lawyer's fee--for example, recovery of property from the client." n7 Recently, the Montana Supreme Court concluded that Rule 1.6 of the Montana Rules of Professional Conduct, which is identical to Model Rule 1.6, contemplates revealing confidential client information by a former in-house lawyer pursuing a retaliatory discharge claim against her former employer. n8 We conclude that a retaliatory discharge or similar claim by an in-house lawyer against her employer is a "claim" under Rule 1.6(b) (2).

n6 MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 4-101(C) (4) (1978).

n7 ANNOTATED MODEL RULES OF PROFESSIONAL CONDUCT 68 (4th ed. 1999).

n8 *Burkhart v. Semitool, Inc.*, 300 Mont. 480, 497, 5 P.3d 1031, 1041 (Mont. 2000).

Only Necessary Information May Be Disclosed



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In pursuing a retaliatory discharge claim, however, the lawyer must limit disclosure of confidential client information to the extent reasonably possible. A comment to Rule 1.6 provides that "[a] lawyer must make every effort practicable to avoid unnecessary disclosure of information relating to a representation, to limit disclosure to those having the need to know it, and to obtain protective orders or make other arrangements limiting the risk of disclosure." n9

n9 Rule 1.6 cmt. [19].

The measures necessary to protect information that may be disclosed will be unique to each situation. For example, a lawyer should consider the protections offered by in camera review at a pre-trial evidentiary hearing. To prevent unnecessary disclosure of confidential information, a lawyer should consider requesting that a court seal the record of the proceedings n10 and consider in an appropriate case whether the action should go forward without disclosing even the names of the parties. n11

n10 See, e.g., *Doe v. A. Corp.*, 709 F.2d 1043, 1045, n.1, reh'g denied, 717 F.2d 1399 (5th Cir. 1983).

n11 Id.

Conclusion

Retaliatory discharge actions provide relief to employees fired for reasons contradicting public policy. The Model Rules do not prevent an in-house lawyer from pursuing a suit for retaliatory discharge when a lawyer was discharged for complying with her ethical obligations. An in-house lawyer pursuing a wrongful discharge claim must comply with her duty of confidentiality to her former client and may reveal information to the extent necessary to establish her claim against her employer. The lawyer must take reasonable affirmative steps, however, to avoid unnecessary disclosure and limit the information revealed.

This opinion is based on the Model Rules of Professional Conduct and, to the extent indicated, the predecessor Model Code of Professional Responsibility of the American Bar Association. The laws, court rules, regulations, codes of professional responsibility, and opinions promulgated in the individual jurisdictions are controlling.

AMERICAN BAR ASSOCIATION STANDING COMMITTEE ON ETHICS AND PROFESSIONAL RESPONSIBILITY, 541 North Fairbanks Court, 14th Floor, Chicago, Illinois 60611-3314 Telephone (312)988-5300 CHAIR: Donald B. Hilliker, Chicago, IL [] Loretta C. Argrett, Washington, DC [] Jackson M. Bruce, Jr., Milwaukee, WI [] William B. Dunn, Detroit, MI [] James W. Durham, Philadelphia, PA [] Mark I. Harrison, Phoenix, AZ [] Daniel W. Hildebrand, Madison, WI [] William H. Jeffress, Jr., Washington, DC [] M. Peter Moser, Baltimore, MD [] CENTER FOR PROFESSIONAL RESPONSIBILITY: George A. Kuhlman, Ethics Counsel; Eileen B. Libby, Associate Ethics Counsel

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Hutchins contended that even if no government money was expended in connection with the law firm's inflated legal bills, the submission of these bills for approval by the bankruptcy court amounted to a "false or fraudulent claim for payment or approval" in violation of Section 3729(a)(1).

The court did not agree. "Although not linguistically implausible, we find no support for this reading from the jurisprudence interpreting the False Claims Act," the court declared.

Case law and the statutory definition of "claim" convinced the court that the False Claims Act seeks to redress only the types of fraudulent activity that cause economic loss to the federal government. Otherwise, any plaintiff would be permitted to sue on behalf of the government when false or misleading statements are made to any government agent, the court pointed out.

"For these reasons, we hold that the submission of false claims to the United States government for approval which do not cause financial loss to the government are not within the purview of the False Claims Act," the court declared.

In dismissing the qui tam claim, the district court stated that the bankruptcy court was merely acting as an intermediary without control over government funds. Although affirming the result, the court of appeals rejected that analysis. The proper inquiry, the court said, is not whether an intermediary controls government funds but whether the defendant causes the intermediary to make a false claim against the government resulting in a financial loss to the treasury.

Hutchins also argued that the firm's submission of fraudulent legal bills to the bankruptcy court constituted a "reverse false claim" in violation of Section 3729(a)(7), which holds liable anyone who knowingly makes a false statement "to conceal, avoid, or decrease an obligation" to pay money to the government. If the government were a creditor to a bankrupt estate, it would suffer economic loss by reason of the estate's paying inflated legal bills, Hutchins contended.

The court expressly refused to address that argument, however, because Hutchins had not pleaded a "reverse false claim" violation.

No Retaliatory Discharge. Hutchins also alleged that the law firm fired him for his investigation and reporting of fraud, in violation of Section 3730(h), a "whistleblower" provision that entitles employees to relief if they are discharged or otherwise discriminated against for investigating or prosecuting a civil action for false claims.

A successful cause of action under this provision, the court said, requires the plaintiff to show that he engaged in "protected conduct," meaning acts done in furtherance of a False Claims Act suit, and that his employer was on notice of the "distinct possibility" of False Claims Act litigation and retaliated against him because of his protected conduct.

The court acknowledged that, in many cases, an employee's internal reporting of fraudulent or illegal activity to an employer may satisfy these requirements. But an employee whose job duties involve investigating and reporting fraud has a heightened burden of proof on these points, the court declared.

Applying these principles, the court found that Hutchins failed to meet the requirements for suing as a whistleblower.

Hutchins's "investigation" came in response to a specific assignment from a partner, not from an independent suspicion of fraud, the court emphasized.

The court also stressed that Hutchins did not tell the firm that he was going to report the problem to government officials or that he was contemplating his own qui tam suit. Furthermore, he did not use the terms "illegal" or "fraud" nor did he attempt to discuss the firm's billing practice with corporate counsel, the court added.

Marianne E. Murphy of Tompkins, McGuire, Wachenfeld & Barry, Newark, N.J., argued for Wilentz, Goldman & Spitzer. Douglas Hallward-Driemeier, Washington, D.C., argued for the United States. Hutchins argued on his own behalf.

Corporate Counsel

Tennessee Court Says In-House Counsel Can't Bring Suit for Retaliatory Discharge

An in-house lawyer who claims that she was fired for reporting her supervisor's lack of a Tennessee law license cannot pursue a claim for retaliatory discharge under Tennessee law even if the claim could be proven without violating the attorney-client privilege, the Tennessee Court of Appeals held June 18 (*Crews v. Buckman Laboratories International Inc.*, Tenn. Ct. App., No. W2000-01834-COA-R3-CV, 6/18/01).

Addressing a question of first impression in the state, the court expressed concern that allowing in-house counsel to pursue a retaliatory discharge claim could chill the relationship between corporate lawyers and their employer-clients.

No Tennessee License. Julia Beth Crews alleged that she was working as an in-house lawyer for Buckman Laboratories International when she discovered that her supervisor—the company's general counsel, Katherine Buckman Davis—was not licensed to practice law in Tennessee.

Crews alleged that when she expressed concern about Davis's licensing status to Joe M. Duncan, an attorney and a member of Buckman's board of directors, Duncan submitted an inquiry to the Tennessee Board of Professional Responsibility, which advised that "a person with a valid license from another state may not be employed as general counsel in Tennessee, unless that person also has a valid Tennessee law license."

Crews alleged that Davis then took the Tennessee bar exam but failed to complete other requirements for a Tennessee law license. Crews claimed that she reported the problem to company officials, consulted independent legal counsel, and informed the board of law examiners, whereupon the work situation deteriorated and Buckman fired her.

Three Views. On appeal from the trial court's dismissal of Crews's wrongful discharge action, the court framed the issue as "whether Ms. Crews has stated a common law claim for retaliatory discharge in violation of the public policy of the State of Tennessee."

In his opinion for the court, Judge W. Frank Crawford noted that under a public policy exception to the at-will employment doctrine in Tennessee, an employee-at-will generally may not be discharged for any reason that violates a clear public policy evidenced

by an unambiguous constitutional, statutory, or regulatory provision. The court decided, however, that "the public policy exception does not apply to the particular facts of this case."

From a survey of the "dozen or so cases from other jurisdictions which have addressed the issue" of retaliatory discharge claims by in-house counsel, the court discerned three basis approaches.

First, the court noted, some jurisdictions allow the cause of action under a breach of contract theory—which Crews did not pursue here—in cases where an employer's statement of company policy has given rise to an implied contract between the employer and the in-house lawyer.

The second approach, the court continued, permits in-house counsel to maintain a claim for retaliatory discharge if the claim can be proven without any violation of the lawyer's obligation to respect client confidences.

The last approach, the court said, is to deny such retaliatory discharge claims. The court cited *Balla v. Gambro Inc.*, 584 N.E.2d 104 (Ill. 1991), as the leading case for this view, and it quoted at length from *Balla*, which it described as "a very well-reasoned opinion."

Public Policy Concerns. In urging the court to permit her retaliatory discharge action, Crews argued that Tennessee has a strong public policy for the regulation of lawyers. The court found that policy to be adequately served, however, by the existing protections of Tennessee statutes and the lawyer ethics code.

"[The] well-established disciplinary requirement [to report ethics violations] is, in and of itself, sufficient to protect the public policy concerns at issue in this case."

TENNESSEE COURT OF APPEALS

In particular, the court noted that a Tennessee statute prohibits the practice of law by nonlawyers, and that DR 3-101(A) of the Tennessee Code of Professional Responsibility prohibits lawyers from aiding nonlawyers in the unauthorized practice of law. Furthermore, the court remarked, DR 1-103(A) requires a lawyer with unprivileged knowledge of a disciplinary rule violation to report it.

Therefore, the court observed, once Crews had knowledge that Davis was engaged in unauthorized practice, she was ethically required to report Davis's conduct. "We believe that this well-established disciplinary requirement is, in and of itself, sufficient to protect the public policy concerns at issue in this case," Crawford stated.

Crews contended that expanding the public policy exception to include in-house counsel would promote lawful conduct by lawyers. The court spurned that argument as incorrectly implying that an in-house lawyer has a choice between complying with disciplinary rules and retaining her job. "No such choice exists," Crawford declared.

The court was equally unpersuaded by the argument that enlarging the public policy exception to include in-

house lawyers would encourage employers to comply with the law. "We believe that, rather than encouraging compliance, such an action could seriously impair the special relationship of trust between an attorney and his or her client," the court said.

A client needs to have complete trust in its lawyer, the court emphasized. It took note of the comment in *Balla* that if lawyers are granted the right to sue their employers for retaliatory discharge, employers might be less willing to be candid with their in-house counsel, especially regarding potentially questionable corporate conduct.

The same logic applies even if the plaintiff-attorney could prove his case without violating attorney-client confidentiality, the court added. "In the unlikely event that the in-house attorney were able to prove retaliatory discharge without violating privilege," the court said, "such a claim might have the effect of chilling the attorney-client relationship."

Finally, Crews suggested that allowing money damages as a remedy for wrongful discharge would not interfere with the employer-client's right to discharge counsel for any reason. But that remedy would still leave the problem of chilling the attorney-client relationship, the court responded. In addition, allowing damages would shift the costs of in-house counsel's compliance with disciplinary rules from the attorney to the employer, Crawford pointed out.

Donald A. Donati and William B. Ryan of Donati Law Firm in Memphis, Tenn., represented Crews. Buckman was represented by Frederick J. Lewis, Thomas L. Henderson, and Whitney K. Fogerty of Lewis, Fisher, Henderson & Claxton, Memphis.

Fees

Fee-Sharing Accord Is Unenforceable Where Split Wasn't Proportional to Services

Fee-sharing agreements not based either on the lawyers' proportion of services rendered or on their assumption of joint responsibility for the representation are void, the New York Supreme Court, Appellate Division, Third Department, made clear in a May 24 ruling (*Ford v. Albany Medical Center*, N.Y. Sup. Ct. App. Div. 3d Dept., No. 88516, 5/24/01).

Justice John A. Lahtinen stressed that the "plain language" of New York's DR 2-107(A)(2) calls for the division of any fee to be in proportion to the services performed by each lawyer when the lawyers do not in writing assume joint responsibility for a client's representation.

Because the lawyers here did not undertake joint accountability for the representation, Lahtinen said, their purported contract for a split not based on the actual share of their services was unenforceable and the fee must be apportioned based on quantum meruit.

Undone Deal. Sandra Ford consulted with attorney Eugene R. Spada in February 1998 about a possible medical malpractice action on behalf of her daughter. Using documents provided by Ford, Spada obtained an expert medical opinion suggesting that Ford had a cause of action for medical malpractice.

On April 8, 1998, attorney Charles R. Harding informed Spada by letter that Ford had retained him to

CONTACTING CURRENT AND
FORMER EMPLOYEES

HUMCO, INC. V. NOBLE



LEXSEE 31 S.W.3d 916

HUMCO, INC., D/B/A HUMANA HOSPITAL-LEXINGTON, APPELLANT v.
HONORABLE MARY C. NOBLE, JUDGE, FAYETTE CIRCUIT COURT, FIFTH
DIVISION, APPELLEE; MARY COLEMAN, REAL PARTY IN INTEREST

2000-SC-0018-MR

SUPREME COURT OF KENTUCKY

31 S.W.3d 916; 2000 Ky. LEXIS 144

November 22, 2000, RENDERED

SUBSEQUENT HISTORY:

[**1] Released for Publication December 13, 2000.

PRIOR HISTORY:

ON REVIEW COURT OF APPEALS. 1999-CA-2027-OA. HONORABLE MARY C. NOBLE, JUDGE, FAYETTE CIRCUIT COURT, FIFTH DIVISION.

DISPOSITION:

AFFIRMED.

CASE SUMMARY

PROCEDURAL POSTURE: Appellant sought review of the decision of the Court of Appeals (Kentucky) denying a petition for a writ of mandamus to direct a trial court to disqualify trial counsel for having ex parte contacts with appellants employees.

OVERVIEW: Attorneys for real party in interest, alleging appellant's racial discrimination, contacted appellant's employees. Correspondence from appellant's employee to the attorneys indicated a copy was sent to appellant's counsel. Real party in interest sued appellant, and appellant sought the disqualification of her attorneys and suppression of notes of interviews, due to the ex parte contacts. The trial court denied this motion. Appellant's petition for a writ of mandamus from the court of appeals was denied. Appellants sought review in the state supreme court. Sending a copy of correspondence to a party's attorney did not establish the attorney represented the party concerning the correspondence. The record did not establish real party in interest's counsel knew appellant was represented concerning her allegations when they contacted appellant's employees. Counsel's contact with appellant's former employ-

ees was not prohibited as those employees' interests were not at stake in the litigation. An attorney's obligation to avoid the appearance of impropriety was adopted to enforce an attorney's duty of loyalty to a former client and did not extend to persons other than clients.

OUTCOME: Court of appeals' denial of writ of mandamus was affirmed because record did not establish real party in interest's counsel knew appellant was represented concerning real party's allegations when they contacted appellant's current employees, and the attorneys were not prohibited from contacting former employees, as they were no longer parties to the litigation.

CORE CONCEPTS**Civil Procedure : Counsel**

Individuals often copy "their attorney" on letters, but that fact alone does not establish that the attorney is representing the letter-writer.

Civil Procedure : Counsel

The requirement in Ky. Sup. Ct. R. 3.130, Rule 4.2 of securing permission of counsel before speaking to someone is limited to those circumstances where the inquiring lawyer knows that the person with whom he wants to speak is represented by counsel with respect to the subject of the communication. Actual knowledge is required and may be inferred from the circumstances.

Civil Procedure : Counsel

Ky. Sup. Ct. R. 3.130, Rule 4.2, entitled "Communication with Person Represented by Counsel," limits an attorney's right to contact the employees of a represented organization.

Civil Procedure : Counsel

See Ky. Sup. Ct. R. 3.130, Rule 4.2.

Civil Procedure : Counsel

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There are three categories of employees of a represented organization that are off limits to opposing counsel: 1) persons having managerial responsibility on behalf of the organization, 2) any other person whose act or omission in connection with that matter may be imputed to the organization for purposes of civil or criminal liability, and 3) any other person whose statement may constitute an admission on the part of the organization.

Civil Procedure : Counsel

Ky. Sup. Ct. R. 3.130, Rule 4.2, restricting employees of an organization with whom an employee may have contact does not distinguish between current and former employees of the organization.

Civil Procedure : Counsel

Ex parte contact with an organization's former employees by an attorney pursuing an action against the organization is not prohibited.

Civil Procedure : Counsel

Ky. Sup. Ct. R. 3.130, Rule 4.2, restricting an attorney's right to have contact with employees of an organization against whom he or she is pursuing an action, does not extend to former employees, even if they are former managerial employees or those whose conduct might have been the basis for imputing liability to the employer or whose statements could be admitted in evidence as an admission by the employer.

Civil Procedure : Counsel

The purpose of Ky. Sup. Ct. R. 3.130, Rule 4.2, restricting an attorney's right to contact employees of an organization represented by counsel, is not to prevent the flow of information, even if damaging to a party in a suit.

Civil Procedure : Appeals : Appellate Jurisdiction : Extraordinary Writs

A writ of mandamus is an extraordinary remedy and should be granted only when the lower court is proceeding or about to proceed without jurisdiction, and there is no adequate remedy by law, or to establish that the lower court, although acting with jurisdiction, is about to act incorrectly and there is no adequate remedy by appeal and great injustice or irreparable injury would result. In deciding the propriety of the denial of a writ, the appellate court must determine whether the lower tribunal exercised sound discretion or acted arbitrarily.

COUNSEL:

FOR APPELLANT: Jeffrey J. Kuebler, KUEBLER LAW OFFICES, Lexington, KY.

FOR APPELLEE, MARY C. NOBLE: Hon. Mary C. Noble, Judge, Fayette Circuit Court. Lexington, KY.

FOR APPELLEE, REAL PARTY IN INTEREST, MARY COLEMAN: Albert F. Grasc, Jr., Theodore E. Cowen, GRASCH & COWEN, P.S.C., Lexington, KY.

ATTORNEY FOR AMICUS CURIAE, THE KENTUCKY ACADEMY OF TRIAL ATTORNEYS: John C. Roach, Robert E. Wier, RANSELL, ROACH & WIER, PLLC, Lexington, KY.

JUDGES:

OPINION OF THE COURT BY CHIEF JUSTICE LAMBERT. All concur, except Wintersheimer, J., who concurs in result only.

OPINIONBY:
LAMBERT

OPINION:

[*918]

OPINION OF THE COURT BY CHIEF JUSTICE LAMBERT

AFFIRMING

Pursuant to CR 76.36(7)(a), Humco, Inc., doing business as Humana Hospital-Lexington ("Humana"), appeals from an order of the Court of Appeals denying its petition for a writ of mandamus. Through the writ, Humco sought to compel Judge Mary C. Noble of the Fayette Circuit Court to disqualify opposing [**2] counsel for allegedly making improper *ex parte* contacts, in violation of SCR 3.130(4.2), with current and former Humana employees and to suppress written statements obtained as a result of these contacts.

The underlying claim involves allegations of racial discrimination by the real party in interest, Mary Coleman, against Humana, her former employer for which she worked as a nurse from 1988 to 1995. In July 1995, prior to suit being filed, Coleman's former counsel, Virginia M. Angellis, wrote to Becky Adams, hospital administrator for Humana, regarding Coleman's discrimination claims. Adams responded in a letter, noting on the letter that it was copied to Humana's legal counsel: "Lois Hess, House Counsel, Jewish Hospital HealthCare Services." The letter indicated that Humana did not tolerate discrimination in its organization and that it had an internal grievance procedure for dealing with discrimination claims.

In September 1995, prior to the commencement of litigation, Angellis contacted five Humana employees regarding the matter. At least four were current employees at the time of contact, and the position and em-



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ployment status of the fifth is unknown. Of these four, three [**3] were staff nurses and one was a staffing coordinator. In her affidavit in this proceeding, Angellis stated that she did not know that Humana was represented by counsel on this matter at the time she undertook the witness interviews. She further stated that she was unaware that Humana was formally represented until March 1996, after suit had been filed and William Rambicure had entered his appearance as counsel for Humana.

In March 1996, Coleman filed suit against Humana. In May 1996, Albert F. Grasc and Theodore E. Cowen of Grasc and Cowen, P.S.C., replaced Angellis as counsel for Coleman, and the new attorneys took possession of the notes prepared by Angellis from her communications with Humana employees. From September 1996 through the winter of 1998, Coleman's counsel contacted approximately ten *former* Humana employees, at both management and non-management levels, without notice to or consent of Humana counsel. Two of these former employees were involved in meetings and discussions regarding the disciplining of Coleman and the ultimate termination of her employment with Humana.

On February 5, 1999, Humana filed a motion in the trial court seeking disqualification of Coleman's [**4] attorneys based upon allegedly improper *ex parte* contacts with current and former Humana employees. In its motion, Humana also requested that the trial court suppress any further use of statements obtained from Humana employees through these contacts. The trial court denied the motion for two reasons. With regard to the current employees Angellis had contacted, the trial court held that the contacts were not improper because the employees were not at a managerial or supervisory level or because the contacts occurred before Humana was represented by counsel. With regard to the former employees contacted by Grasc and Cowen, the trial court held such contact is not prohibited by SCR 3.130(4.2), regardless of whether the employees were at management level or otherwise.

Humana then filed a petition for a writ of mandamus in the Court of Appeals, seeking to compel the trial court to disqualify Grasc and Cowen and to suppress the statements they had obtained. The Court of Appeals denied the writ, holding with regard to the Angellis contacts that there was no evidence that Humana was [**919] formally represented by counsel at that time and that the July 1995 letter to Angellis, copied to Humana's [**5] in-house counsel, was insufficient to put Angellis on notice that Humana was represented by counsel. In support of this conclusion, the Court of Appeals relied upon *K-Mart v. Helton*, n1 which held that the knowledge that

corporations have in-house counsel is not sufficient to provide actual notice of representation.

n1 *Ky.*, 894 S.W.2d 630 (1995).

The Court of Appeals further held that the second set of contacts, between Coleman's current counsel and former Humana employees, were not improper because contact with former employees is not prohibited. In support of this result, the Court of Appeals adopted Formal Ethics Opinion, KBA E-381, which states that communications with unrepresented former employees of an organizational party do not violate SCR 3.130(4.2).

Humana now contends, relying on *Shoney's Inc. v. Lewis*, n2 that the contacts made by Angellis with current employees were improper as Humana was represented by counsel at the time. Humana maintains that the letter sent by Adams [**6] to Angellis and copied to Humana's in-house counsel makes such representation clear. In *Shoney's*, the plaintiff's counsel was explicitly advised that the defendant corporation was represented by counsel and was given the name of such counsel. No such explicit information was conveyed to Angellis in this case. Adams' letter did not state that Humana was represented by an attorney nor state that all further contact was to be through Hess. Adams' letter did not state that Hess was to be consulted in the matter.

n2 *Ky.*, 875 S.W.2d 514 (1994).

Individuals often copy "their attorney" on letters, but that fact alone does not establish that the attorney is representing the letter-writer nor does this record reveal any such representation. n3

n3 See *K-Mart v. Helton*, *supra*; *Miano v. AC&R Advertising, Inc.*, 148 F.R.D. 68, 80 (S.D.N.Y. 1993) ("mere existence of general counsel, without particular involvement in the matter at issue, is insufficient to render a corporation 'represented'").

[**7]

This conclusion is supported by a Formal Opinion of the American Bar Association, No. 95-396. This opinion states that the requirement in Rule 4.2 of "securing permission of counsel is limited to those circumstances where the inquiring lawyer 'knows' that the person with whom he wants to speak is represented by counsel with respect to the subject of the communication." The opinion further states that actual knowledge is required and may be inferred from the circumstances. n4 Such circumstances are not present in this case, as there is no



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evidence from the record that Humana was formally represented by Hess when the communications occurred or that Angellis knew that Humana was represented by counsel.

n4 ABA Formal Opinion 95-396 at 12-13.

With regard to former managerial employees, Humana urges this Court to hold that such contacts should be prohibited if they concern the subject of representation and if the former employee has personal knowledge of the matter that could be imputed to the employer. With regard [**8] to former non-managerial employees, Humana argues that contact should be prohibited if an employee's acts or omissions may be imputed to the organization or if their statements may constitute admissions by the organization. To resolve the issue of whether confidential information should remain confidential regardless of whether the individual is still employed, it is necessary to review the rule, its rationale, and interpretations thereof.

SCR 3.130, Rule 4.2, entitled "Communication with Person Represented by Counsel," limits an attorney's right to contact the employees of a represented organization. Specifically, the rule provides:

[*920] In representing a client, a lawyer shall not communicate about the subject of the representation with a party the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized by law to do so.

The official commentary to the rule explains that there are three categories of employees of a represented organization that are off limits to opposing counsel: 1) persons having managerial responsibility on behalf of the organization, 2) any other person whose act or omission [**9] in connection with that matter may be imputed to the organization for purposes of civil or criminal liability, and 3) any other person whose statement may constitute an admission on the part of the organization.
n5

n5 See *Shoney's v. Lewis, Ky.*, 875 S.W.2d 514, 515 (1994) (citing SCR 3.130, Rule 4.2, comment 2).

The rule does not distinguish between current and former employees of the organization. As noted by the Court of Appeals, Formal Ethics Opinion KBA E-381 provides guidance in this area. In holding that *ex parte* contact with an organization's former employees is not prohibited, the ethics opinion reasoned, "a former employee is no longer subject to the control of the organiza-

tion nor in a position to speak for the organization, and cannot make vicarious admissions under the state and federal evidence rules." The opinion refers to a formal opinion issued in 1991 by the American Bar Association Committee on Ethics and Professional Responsibility, which explicitly states that [**10] Rule 4.2 does not extend to former employees, even if they are former managerial employees or those whose conduct might have been the basis for imputing liability to the employer or whose statements could be admitted in evidence as an admission by the employer. n6

n6 ABA Committee on Ethics and Professional Responsibility, Formal Op. 91-359, at 6 (March 22, 1991).

We believe this to be the sound approach and observe that it has been adopted by the majority of other jurisdictions. The majority rule is consistent with the purposes and policies of Rule 4.2. The purpose of Rule 4.2 is not "to prevent the flow of information, even if damaging to a party in a suit." n7 Rather, it is to preserve the positions of the parties in an adversarial system and thereby to maintain the protections obtained by employing counsel and prevent disruption of the attorney-client relationship. A former employee with no present relationship with the organizational party is not a "party" under the rule, and thus the individual is not [**11] adverse in the sense that his interests are at stake in the litigation.

n7 *Aiken v. The Business and Industry Health Group, Inc.*, 885 F. Supp. 1474, 1479 (D. Kansas 1995).

Finally, Humana argues that the Court of Appeals should be reversed and the writ of mandamus granted because, even if no technical ethical violation occurred, Coleman's attorneys have created an impermissible appearance of impropriety. n8 This standard has been adopted as a basis independent of SCR 1.9 for enforcing an attorney's duty of loyalty and confidentiality to a former client to avoid compromise by subsequent representation of another party. n9 Lovell is clearly limited to protecting the attorney/client relationship or the reasonable expectations of parties in that regard and to promoting public confidence in the integrity of the legal profession. We decline the invitation to extend this standard to situations involving transactions with persons other than clients under SCR 4.2.

n8 *Lovell v. Winchester, Ky.*, 941 S.W.2d 466 (1997).

[**12]

n9 941 S.W.2d 466 at 468-469.

A writ of mandamus is an extraordinary remedy and should be granted only when the lower court "is proceeding or about to proceed without jurisdiction, and there is no adequate remedy by law, or to establish that the lower court, although [*921] acting with jurisdiction, is about to act incorrectly and there is no adequate remedy by appeal and great injustice or irreparable injury would result." n10 In deciding the propriety of the denial of a writ, this Court must determine whether the Court of Appeals exercised sound discretion or acted arbitrarily. n11 Here, we are compelled to conclude that the Court of Appeals' decision was not arbitrary and that

it acted properly in denying Humana's request for a writ ordering disqualification of opposing counsel.

n10 *Bock v. Graves, Ky., 804 S.W.2d 6, 9 (1991).*

n11 *Jones v. Hogg, Ky., 639 S.W.2d 543 (1982).*

[**13]

For the foregoing reasons, the judgment of the Court of Appeals is affirmed.

All concur, except Wintersheimer, J., who concurs in result only.