Employer ALERTS!

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"Friends" Still Airing in Court

By Charles H. Fleischer, Esq.

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.

The long-running series "Friends" may be over for most viewers, but it is still playing in the California courts.

When Amaani Lyle, an African-American woman, learned that the producers of the show were looking for writers' assistants, she applied and was hired. She knew at the time that one of her most important duties would be to attend writers' meetings and take copious, detailed notes while the writers were discussing story lines, jokes and dialogue. She also knew she would be expected to be a fast typist. She was fired after four months, allegedly for poor performance.

After being discharged, Lyle sued Warner Brothers and the writers and producers for sexual harassment under California's employment discrimination law. Her testimony describes meetings during which the writers pretended to engage in sexual activity, and they discussed their sex lives and preferences and their fantasies about the actresses on the show. According to Lyle, this conduct occurred nearly every working day during the four months she was employed on the show.

Lyle's employers responded to the suit with a defense of "creative necessity." They claimed that while the writers' behavior might support a sexual harassment suit in other contexts, it could not support liability here because the writers were only doing their job. The writers' job, they explained, was to create jokes, dialogue and story lines for an adult-oriented situation comedy. Because "Friends" dealt with sexual matters, intimate body parts and risqué humor, the writers were required to have frank sexual discussions and tell colorful jokes and stories, and even make expressive gestures, as part of the creative process.

A California appellate court accepted the creative necessity defense *in part*. The court ruled that while the defense would not justify outright dismissal of Lyle's claim, the defense could be argued to a jury at trial. The court pointed out that the context in which alleged harassment occurs is relevant in determining whether the conduct is sufficiently severe or pervasive to create an objectively hostile work environment. Quoting an earlier U.S. Supreme Court decision, the court said that the real social impact of workplace behavior often depends on a constellation of surrounding circumstances, expectations and relationships which are not fully captured by a simple recitation of the words used or the physical acts performed.

The case is on further appeal to the California Supreme Court.

Reference: *Lyle v. Warner Bros. Television Productions*, 12 Cal.Rptr.3d 511 (Cal.App. 2003), *pet. for review granted* (Cal. No. S125171, July 21, 2004).

ERISA Retaliation

The Employee Retirement Income Security Act, which regulates employee benefit plans, makes it unlawful to discharge, discipline, or discriminate against a plan participant or beneficiary for exercising any right to which he or she is entitled under a plan or for giving information or testifying in connection with an ERISA inquiry. It is also unlawful under ERISA for an employer to interfere with the attainment of any right to which a participant may become entitled under the plan. This means that an employer cannot fire an employee in order to prevent him or her from becoming vested in a retirement plan or in order to reduce the amount of benefits that might otherwise be available.

Two cases show how this anti-retaliation provision works.

Heath v. Varity Corp

A Wisconsin farm equipment manufacturer fired one of its employees after he had worked there almost 30 years and shortly before he was to become eligible for early retirement. The discharge did not affect his basic pension, which was fully vested, but it did prevent him from becoming eligible for certain additional benefits.

Believing that the company acted for the purpose of interfering with attainment of those additional benefits, the employee sued under ERISA. The trial court dismissed the suit, reasoning that the benefits at issue were not then vested and since the employer retained the power to amend the plan and eliminate those benefits entirely, it necessarily had the power to fire the employee to prevent him from attaining the benefits.

A federal appeals court reversed and sent the case back for trial. The appellate court ruled that ERISA protects unvested as well as vested benefits and that the power to amend a plan does not allow an employer to interfere with a particular employee's benefits, whether vested or not.

Fields v. Thompson Printing

Gerald Fields began work at a New Jersey printing company when he was 13 and came to own 20% of its stock. In 1990, after Fields had been on the job for 35 years, the company offered him 10-year, "no-cut" contract, guaranteeing him a 10% annual raise during the life of the contract, a new car every four years, various other benefits, and a retirement payment of $2,000 per week. In the event the company terminated Fields, his benefits were to continue for the remainder of the term. Only if Fields voluntarily quit could the company discontinue his benefits under the contract.

In 1997, three female employees accused Fields of sexually harassing them. In response, the company president telephoned Fields, who was on vacation with his family at the time, and fired him. The three female employees later filed a sex discrimination lawsuit against the company, Fields, and other supervisors, but their case was settled without any findings or admissions of wrongdoing. Nevertheless, the company refused to pay contract benefits to Fields.

Fields sued, claiming that the Company violated ERISA and the terms of his employment contract when it refused to continue paying benefits. The company responded that Fields' alleged acts of sexual harassment breached the employment agreement, which excused the company from further performance. In addition, said the company, enforcement of the agreement would violate public policy because it would, in effect, interfere with the company's efforts to prevent sexual harassment.

A federal appeals court sided with Fields, ruling that the company must comply with the contract. The court first noted that the allegations of sexual harassment had never been proved. But even if the allegations had been proved, the contract did not distinguish between a termination without cause and a termination for cause; the only event relieving the company of its obligation would be Fields' voluntary quit.

As to the company's public policy argument, the court ruled that the contract's payment provisions were perfectly legal and no public policy would be offended by enforcing them. Finally, since the post-termination benefits provided by the contract were subject to ERISA, failure to pay those benefits amounted to an ERISA violation.

References: 29 U.S.C. § 1001, *et seq.; Heath v. Varity Corp.*, 71 F.3d 256 (7th Cir. 1995); *Fields v. Thompson Printing Co.*, 363 F.3d 259 (3rd Cir. 2004).

Remedies for Discrimination

An unsuccessful candidate for employment who feels he or she has been rejected for discriminatory reasons may notify the employer involved and ask for reconsideration. More likely, the candidate will go straight to a local office of the Equal Employment Opportunity Commission (EEOC), or to a state or local fair employment practices agency (FEPA), and file a formal charge of discrimination. For most types of discrimination prohibited by federal law, filing a charge with the EEOC or a FEPA is a prerequisite to suing in court.

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.
7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814
T: 301-656-5700 F: 301.951-0555 www.OFQ Law.com

Often the EEOC and a state or local FEPA will each have jurisdiction over a particular charge. When that is the case, the charge will be dual filed – whichever agency first receives the charge will transmit a copy to the other agency. Normally the agency that first receives the charge will take the lead in handling the charge; work sharing agreements between the EEOC and the FEPA may provide otherwise, however.

A charge of discrimination must be filed with the EEOC within 180 days after the alleged discrimination occurred. If the charge is also covered under state or local discrimination laws, then the 180-day time limit is extended to 300 days.

Processing a Charge

On receipt of a charge, the EEOC will first determine whether it has jurisdiction – that is, whether the type of discrimination being charged, if in fact it occurred, would violate federal law; whether the charging individual is an employee or candidate for employment; and whether the employer has a sufficient number of employees to meet any applicable threshold. If the EEOC has jurisdiction, it will then notify the employer of the charge and begin an investigation.

Often the first time an employer becomes aware that it has been accused of discrimination is when the employer receives a Notice of Charge of Discrimination, EEOC Form 131. The Notice will normally include a copy of the charge itself and it will identify the type of discrimination being charged (race, age, disability, etc.). It is usually in the employer's best interest to cooperate with the EEOC at this juncture. (If the EEOC serves the employer with a subpoena for documents and records, non-cooperation may not be an option.)

Typically, the EEOC will request the employer to file a *position statement* stating the employer's position with respect to the charge. The EEOC's investigation may also include a request for employer documents and records, an on-site inspection, and interviews of other employees. If the EEOC concludes that no discrimination has occurred, the EEOC will notify the parties, close its case, and issue a *right-to-sue* letter to the employee. If the EEOC concludes that discrimination has occurred, the parties will be informed and the EEOC will attempt to conciliate the matter by seeking the parties' agreement on appropriate remedies. If the conciliation is successful, that will end the matter unless one of the parties later violates the conciliation agreement.

If conciliation is unsuccessful, the EEOC will either issue a right-to-sue letter to the employee, or it may decide to bring suit itself against the employer. The EEOC may decide to sue as plaintiff if, for example, the case involves an important but unresolved legal principle, or if the case involves a large number of employees.

For most types of discrimination, an employee has 90 days after receiving a right-to-sue letter to file suit in court. If the claim involves a violation of federal discrimination laws, suit can be brought either in federal district court or in state court. If only state or local discrimination laws are involved, the victim will normally be limited to suing in state court.

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7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814
T: 301-656-5700 F: 301.951-0555 www.OFQ Law.com

Available Remedies

Once discrimination is found, a wide variety of remedies is available under federal law. These may be classified as *victim-specific remedies*–that is, remedies that are intended to make the victim whole by placing the victim in the position he or she would have been in but for the discrimination; and general remedies, which are focused on curing faulty workplace practices.

Victim-specific remedies include:

- requiring the employer to *hire* the rejected candidate (and to provide reasonable accommodation, in cases of disability discrimination);
- awarding the victim *back pay* (the pay he or she would have received between the time of the discrimination and the date of the award);
- when hiring or re-hiring the individual is not feasible, awarding *front pay* (the pay the victim would have received from the time of the award to some reasonable time in the future);
- awarding *compensatory damages* (which can include damages for emotional pain and suffering);
- awarding *punitive damages* to punish the employer;
- requiring the employer to pay the victim's *attorneys' fees, expert witness fees* and *court costs*.

A party seeking compensatory or punitive damages is entitled to a jury trial. However, the amount of compensatory and punitive damages that may be awarded under federal law is subject to the following dollar limitations, or caps, depending on the number of employees the employer has:

Number of employees	Cap
Between 15 and 100	$ 50,000
Between 101 and 200	$100,000
Between 201 and 500	$200,000
More than 500	$300,000

Note, however, that back pay and front pay claims are not subject to these caps.

General remedies (remedies that are not victim-specific) include an injunction, which forbids the employer from discriminating in the future; a requirement that the employer post notices in the workplace concerning the violation and employees' rights under the law; and a requirement that the employer provide training or take other measures to prevent future discrimination and submit compliance reports to the EEOC

State and local discrimination laws provide similar remedies, but without the caps. For that reason, victims will often combine both federal and state or local claims in their suits.

Employees who have been fired for discriminatory reasons cannot, of course, just sit back and let their claims for back pay and front pay accumulate. Instead, as the following case illustrates, they have an obligation to mitigate their damages – that is, to pursue gainful employment.

Johnson v. Spencer Press

After Albert Johnson received a bachelor's degree in Bible studies he worked as a church pastor and later in a school for the mentally retarded. He then left active ministry and took a job as a custodian at a printing company in Maine, but he remained very religious. Johnson's supervisor at the printing company learned about Johnson's religious views when Johnson asked for Sundays off. Apparently having a low regard for those views, the supervisor embarked on an eight-year campaign of ridiculing Johnson, his religion, his strict sobriety, and his unwillingness to womanize. The supervisor's harassment included obscene references to Christian religious figures. Johnson's complaints to Human Resources were unavailing, so Johnson finally quit, which the court treated as a constructive discharge. Johnson was quickly able to obtain replacement work at a supermarket, but he was fired from the supermarket job shortly thereafter for violating a rule against eating food that had not been paid for.

In Johnson's suit against the printing company for religious discrimination, a jury awarded him $1,150,000 in compensatory and punitive damages, which the court reduced to the statutory cap of $300,000. However, the court would not allow the jury to award back pay or front pay past the date Johnson was fired from his supermarket job, ruling that Johnson had failed to mitigate his damages. In other words, Johnson's own misconduct at the supermarket, not his constructive discharge by the printing company, caused his subsequent lost wages.

Reference: *Johnson v. Spencer Press of Maine, Inc.*, 364 F.3d 368 (1st Cir. 2004).

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C. T: 301-656-5700 F: 301.951-0555 www.OFQ Law.com
7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814

Update on Employer Liability for Supervisor's Harassment

Employer liability for a supervisor's workplace sexual harassment continues to be controversial, sometimes producing complicated and less-than-helpful judicial rulings.

Back in 1998 the Supreme Court issued two decisions, known as *Ellerth* and *Faragher*, which set out rules for employer liability for a supervisor's misconduct based on whether or not the victim suffered a tangible employment action. For example, if the supervisor demotes a subordinate because she refuses to sleep with him, the supervisor is exercising authority given by the employer and the employer is *always* liable for the misuse of that authority. However, if the harassment takes the form of a supervisor-created, sexually hostile work environment, but without any tangible employment action, then the employer may be liable, but the employer has the opportunity to defend by showing that (1) it had an effective policy against sexual harassment, and (2) the employee unreasonably failed to take advantage of that policy.

What is a tangible employment action? In *Ellerth* and *Faragher* the Supreme Court defined the term as a "significant change in employment status, such as hiring, firing, failing to promote, reassignment with significantly different responsibilities, or a decision causing a significant change in benefits." As helpful as that definition may be, it is not always easy to apply it.

Pennsylvania State Police v. Suders

In June 2004 the Supreme Court considered the issue again in a case involving Nancy Suders, an employee of the Pennsylvania State Police. Suders claimed that she had been sexually harassed by her supervisor to the point where she had no choice but to quit. At no time prior to quitting, however, had Suders complained to her employer or given her employer an opportunity to address the problem. In her subsequent lawsuit, the employer attempted to raise the *Ellerth/Faragher* defense – that the employer had a policy against sexual harassment and that the employee unreasonably failed to take advantage of it. Suders argued that the defense was unavailable here because she had been constructively discharged – in effect, forced to quit – and that a constructive discharge is a tangible employment action.

On the question whether a constructive discharge is a tangible employment action, the Supreme Court answered that it depends on whether the supervisor's conduct precipitating the constructive discharge was official conduct or unofficial conduct. This question, in turn, depends on whether the specific conduct that triggered the constructive discharge was conduct that only someone in a supervisory capacity could have committed (in which case it would be official conduct and the *Ellerth/Faragher* defense would be unavailable), or whether the specific conduct could have been committed equally easily by a non-supervisory co-worker (in which case the conduct would be unofficial and the *Ellerth/Faragher* defense would still be available). The Court sent the case to back to the lower courts for a determination of this question.

McCurdy v. Arkansas State Police

An interesting twist on the *Ellerth/Faragher* defense recently arose in another case involving state police, this time in Arkansas. Jamie McCurdy worked as a radio dispatcher in Little Rock, assigned to an evening shift. While at work one Friday night, she was allegedly subjected to verbal and physical harassment by a sergeant during a one-hour period. McCurdy promptly reported the incident to another officer, who in turn reported it to higher-level officials.

By Monday, the sergeant had been reassigned so as to prevent further contact with McCurdy. The Internal Affairs Unit then conducted an investigation, concluded that the sergeant had violated workplace rules, and recommended that he be demoted and placed on probation. A disciplinary review board considered those recommendations, conducted further investigation, and submitted its own report to the commanding officer. Based on those investigations and recommendations, the commanding officer discharged the sergeant for sexual harassment and for lack of truthfulness during the investigative process. On further appeal, the State Police Commission overruled the termination, but it approved the sergeant's transfer and demotion.

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7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814
T: 301-656-5700 F: 301.951-0555 www.OFQ Law.com

McCurdy sued the State Police for sexual harassment arising out of the one-hour incident. When the State Police invoked the *Ellerth/Faragher* defense, McCurdy argued that the defense wasn't available because she had not unreasonably failed to take advantage of her employer's non-discrimination policy. To the contrary, she immediately complained about the sergeant's conduct.

The U.S. Court of Appeals for the Eighth Circuit conceded that the second prong of the *Ellerth/Faragher* defense was not satisfied here. Yet, said the court, it would make no sense hold the State Police liable when it did exactly what the discrimination laws were intended to promote: prompt investigation of complaints, and appropriate remedial action if warranted. In cases like this, of a single incident of harassment where no tangible employment action is involved, the second prong of the two-pronged *Ellerth/Faragher* defense is inapplicable, said the court, and the employer is permitted to defend by showing it promptly investigated and took appropriate remedial action.

McDowell v. Calvin Presbyterian Church

Special rules apply to religious organizations. The First Amendment to the U.S. Constitution says that "Congress shall make no law respecting the establishment of religion, or prohibiting the free exercise thereof." Based on the First Amendment, the courts have developed the so-called *ministerial exception* to Title VII, under which religious organizations may discriminate in connection with the selection and employment of their own clergy. See "Federal Non-Discrimination Laws and the 'Ministerial Exception,'" EMPLOYER ALERTS!, Feb. 2001, p. 1. The ministerial exception has its limits, however, as this last case shows.

An ordained female minister was hired as associate pastor for a Presbyterian Church in Washington State. After taking the position, she was allegedly subject to harassment by her supervising pastor. When she complained to higher church authorities, she was suspended without pay and then fired. Church authorities also prohibited her from circulating her résumé to other churches, effectively barring her from employment in any Presbyterian church in the U.S.

The minister sued for sex discrimination and retaliation, but the Church defended on First Amendment grounds, claiming that court involvement in its employment decision would amount to an unconstitutional interference with religion. The trial court agreed with the Church and dismissed the suit, but a federal appeals court reversed. The appellate court recognized that a religious organization's decision to employ or terminate a minister is at the heart of its religious mission. Therefore, the minister could not base her claims on the allegation that she was suspended and then fired in retaliation for her harassment complaint. However, she *could* sue the Church for emotional damages caused by the alleged harassment itself. The appellate court reached its conclusion because the factual issues involved in that claim – whether the minister was in fact harassed, and whether the Church responded reasonably to stop the harassment after she complained – do not intrude on religious doctrine.

References: 42 U.S.C. § 2000e, *et seq.; Burlington Industries, Inc. v. Ellerth*, 524 U.S. 742 (1998); *Faragher v. City of Boca Raton*, 524 U.S. 775 (1998); *Pennsylvania State Police v. Suders*, 124 S.Ct. 2342 (2004); *McCurdy v. Arkansas State Police*, 2004 WL 1636429 (2004); *McDowell v. Calvin Presbyterian Church*, 2004 WL 1636927 (2004).

What Is Adverse Employment Action Under Discrimination Laws?

As stated in the previous article, a "tangible employment action" for purposes of discrimination law is a significant change in employment status. Some actions by an employer, although seemingly adverse, might be so trivial as not to amount to discrimination. A recent case decided by the U.S. Court of Appeals for the Fourth Circuit (which hears federal appeals in Maryland and Virginia) offers additional guidance on the meaning of "significant" in this context.

Aaron James is an African-American electrical engineer employed by Booz-Allen & Hamilton. He was assigned as project manager of a contract Booz-Allen had with the Washington Metropolitan Area Transit Authority (WMATA). Under the contract, James provided engineering services to WMATA in connection with acquisition of new rail cars for the Washington subway system. During James's three-year tenure in that position the contract grew from $1 million annually to $10 million, with James supervising up to 30 employees.

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7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814
T: 301-656-5700 F: 301.951-0555 www.OFQ Law.com

As project manager, James received mixed evaluations, ranging from “excellent” to “effective.” (Under the company’s rating system, “excellent" was the highest followed by “highly effective," then “effective.”)The evaluation forms also noted that he needed to refine his client-handling skills and build stronger relationships with key WMATA officials.

As James’s duties grew, Booz-Allen’s performance, and relations between James and WMATA, deteriorated. WMATA expressed concerns and James responded to those concerns with a memo blaming his counterpart at WMATA. In another incident, James bypassed established channels of communication and contacted a senior executive at WMATA concerning a contract matter. This second incident was resolved by an apology from Booz-Allen to WMATA. Booz-Allen also received complaints as to the timeliness and effectiveness of its work-product.

Eventually, Booz-Allen decided to reassign James, replacing him with a white male. James’s new position involved marketing, not management, but it was otherwise equivalent in terms of prestige, compensation, level of responsibility and benefits. James continued to receive salary increases and bonuses in his new position, and he was given a “highly effective” rating.

Disliking his new position, James filed a race discrimination charge against his employer. His claim was dismissed by the federal court in Alexandria, and the dismissal was affirmed on appeal. The Fourth Circuit ruled that Booz-Allen had not discriminated against James, since the mere fact that a new job assignment was less appealing to the employee does not constitute an adverse employment action. Quoting its own earlier decision in another case, the appellate court said: “Absent any decrease in compensation, job title, level of responsibility, or opportunity for promotion, reassignment to a new position commensurate with one’s salary level does not constitute an adverse employment action even if the new job does cause some modest stress not present in the old position.”

References: 42 U.S.C. § 2000e, *et seq.; James v. Booz-Allen & Hamilton, Inc.*, 368 F.3d 371 (4th Cir. 2004).

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Design: Orange*Zebra*Design KK@OrangeZebra.net

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Bethesda, MD 20814

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Tax Law Changes Could Promote Employee Claims

By Charles H. Fleischer, Esq.

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.

Prior to 1991, the federal civil rights laws allowed employees who suffered workplace discrimination only limited types of relief. For example, a court might order that an employer reinstate an illegally discharged employee and reimburse him for the wages he lost. The court might also issue an injunction against future discrimination by the employer.

In 1991 the civil rights laws were amended to allow recovery of compensatory and punitive damages. See "Remedies for Discrimination," EMPLOYER ALERTS!, Summer 2004, p. 2. That change made civil rights litigation more profitable for both employees and their attorneys and it has undoubtedly contributed to the volume of workplace-related cases in the courts.

Until recently, however, one aspect of the tax laws discouraged such cases. Most damage awards or settlement payments in employment dispute situations constitute taxable income to the employee, and that factor is not likely to change. What is changing is the tax treatment of attorney fees paid to the employee's attorney. Consider this example:

> An employee sues his former employer for discrimination and is awarded $85,000. Since the employee and his attorney have a contingent fee agreement requiring the employee to pay 40% of the total recovery, the employee pays his attorney $34,000 and keeps a net of $51,000. Which of these amounts is taxable income to the employee – the full $85,000? or only the $51,000 the employee got to keep?

To date, the IRS and most courts have concluded that the full $85,000 is taxable income. So if the employee is in the 35% tax bracket, his net, after-tax recovery is only $21,250. Of course, the employee may be able to take a miscellaneous deduction for a portion of the attorney fee payment, but the deduction is only available if the employee itemizes. And even if the employee does itemize, other limitations may reduce the deduction or eliminate it entirely.

It is not unusual in discrimination litigation for a court to order the employer to pay the employee's attorney fees. Suppose, as another example, the court awards $85,000 in damages to the employee and $150,000 to the attorney based on the difficulty of the case and the amount of time the attorney had to spend to win it. In this situation, the employee will have taxable income of $235,000, even though he only gets $85,000. If the employee is in the 40% income tax bracket, he will owe $94,000 in taxes, meaning that, even though he won the case, he collects nothing and will have to come up with $9,000 from his own pocket to pay the tax!

This peculiar tax result serves as a disincentive to employee suits against employers. But the disincentive has now been changed.

The American Jobs Creation Act of 2004, signed by President Bush on October 22, 2004, has a section which excludes from gross income the fees and costs paid in connection with unlawful workplace discrimination claims. This means that an employee will not have to pay tax on the fees paid to his attorney, whether or not the employee itemizes his deductions and whether or not deductions are subject to other limitations.

The Act includes within its definition of "unlawful discrimination" matters covered by Title VII of the Civil Rights Act (race, color, religion, sex, or national origin), the Age Discrimination in Employment Act, and the Americans with Disabilities Act. It also includes claims under a long list of other federal laws relating to the workplace, such as the Fair Labor Standards Act, the Family and Medical Leave Act, the Employee Polygraph Protection Act, the Worker Adjustment and Retraining Notification Act, the National Labor Relations Act, and the various federal whistleblower laws. A final catchall provision allows exclusion of attorney fees in connection with suits under any provision of Federal, State, or local law, or common law claims permitted under Federal, State, or local law – (i) providing for the enforcement of civil rights, or (ii) regulating any aspect of the employment relationship, including claims for wages, compensation, or benefits, or prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation against an employee for asserting rights or taking other actions permitted by law.

The Act applies to fees paid after the effective date of the Act with respect to judgments or settlements occurring after the effective date.

In a related matter, the Supreme Court on November 1, 2004, heard argument on two cases involving the same tax question. Whatever the Court ultimately decides, the impact of its decision is likely to be much less significant in light of the tax law change made by the American Jobs Creation Act of 2004.

References: 26 U.S.C. §§ 62, 104; PLR 200041022
Commissioner v. Schleier, 515 U.S. 323 (1995)
Commissioner v. Banks, 345 F.3d 373 (6th Cir. 2003), *cert granted,* Mar. 29, 2004, No. 03-892, *Commissioner v. Banaitis,* 340 F.3d 1074 (9th Cir. 2003), *cert. granted,* Mar. 29, 2004, No. 03-907, American Jobs Creation Act of 2004, H.R. 4520 (108th Cong., 2d Sess.) (approved Oct. 22, 2004)

Should Your Company Have a Code of Ethics?

Under the Sarbanes-Oxley Act of 2002, publicly-traded companies must report to the Securities and Exchange Commission whether they have adopted a Code of Ethics for their senior financial officers and, if they haven't, why they haven't.

But even if your company is not publicly traded, it is a good idea to have a corporate Code of Ethics for employees, covering the president on down, and to offer periodic training in implementing the Code.

Having and enforcing a corporate Code of Ethics may even provide a measure of protection if your company is accused of criminal misconduct. Criminal liability can attach to an organization whenever an employee of the organization commits an act within the apparent scope of his or her employment, even if the employee acted directly contrary to company policy and instructions. An entire organization, despite its best efforts to prevent wrongdoing in its ranks, can still be held criminally liable for any of its employees' illegal actions. Under the Federal Sentencing Guidelines of the United States Sentencing Commission (a federal agency charged with establishing criminal sentencing guidelines for federal courts), one of the mitigating factors a court will consider in sentencing an organization is whether the organization has an effective compliance and ethics program.

For a Code of Ethics to be effective for purposes of the Federal Sentencing Guidelines, the company must, at a minimum, meet these seven criteria:

- The company must establish standards and procedures to prevent and detect criminal conduct.
- The company must task high level personnel with overall responsibility for overseeing the ethics program.
- The company must make reasonable efforts to exclude from senior management persons who have engaged in criminal or unethical activity.
- The company must conduct periodic training programs on the standards and procedures covered by the ethics program.
- The company must monitor and evaluate its ethics program, it must establish and publicize an anonymous or confidential reporting mechanism, and it must assure that persons who utilize the reporting mechanism do not suffer retaliation.
- The company must enforce its Code of Ethics by providing appropriate incentives for compliance and appropriate discipline for violations.
- The company must respond appropriately once criminal conduct has been detected to prevent future incidents.

What should be included in a company's Code of Ethics? The Code will have to be tailored to each company's specific situation, the industry in which it is involved, the types of employees it has, the geographic areas or countries in which it does business, etc. However, the topics listed below deserve consideration at the least, and will probably be applicable in most situations:

Compliance with Criminal Laws

The Code should require employees, while at work or on company business, to comply with criminal laws generally. These would include:

- crimes against property, such as theft and fraud (including computer fraud, chain letter schemes, denial-of-service attacks, etc.);
- crimes against persons, such as assaults, threats of violence, extortion, blackmail, and crimes involving the possession or use of dangerous weapons; and
- other crimes relating to such activities as gambling, the possession, use or distribution of illegal substances, and possession or transmission of child pornography.

Violations of Co-Employees and Applicants' Rights

A variety of workplace laws protect the rights of employees generally. The Code should require employees to observe applicable

- discrimination laws;
- labor laws, which protect concerted activities of employees;
- health and safety laws;
- laws protecting employee privacy;
- laws relating to immigration and employment of undocumented workers; and
- laws against retaliation for filing complaints, whistleblowing, etc.

Conflicts of Interest

Employees should be prohibited from

- engaging in any type of activity in competition with the company;
- performing work for the company's customers on their off-hours;
- having a personal financial interest in a competitor of the company or otherwise assisting a competitor; and
- serving on boards of customers or vendors where doing so could give the appearance of a conflict of interest.

Company Property

The company should require its employees to safeguard the company's own property, including both its physical assets and its intellectual property. Obviously, direct theft from the company is unacceptable. So are more subtle activities listed here:

- using company supplies and facilities for personal (or, worse, competitive) purposes;
- carrying phantom employees; and
- disclosing trade secrets.

Economic Crimes

Economic crimes include

- insider trading (trading in the stock of the company itself or in the stock of other companies based on information not generally available to the public);
- tipping off family, friends, or others to insider information that could be of value in buying or selling stock;
- fixing bids or sharing pricing or cost information or marking plans with competitors;
- entering into price-fixing agreements with competitors or agreeing to a division of customers or territories between the company and a competitor;
- unauthorized copying of copyrighted materials, including software and images available on the Internet;
- violating patent rights;
- violating license restrictions on third-party computer programs;
- disclosing confidential third-party information or engaging in reverse-engineering in violation of agreements the company may have with partners, vendors or customers;
- acquiring trade secrets from competitors through improper means, such as by theft, bribery or illegal computer access;
- interfering with a competitor's known contractual rights; and
- participating in illegal boycotts.

Relations with Customers and Vendors

Aside from illegality, the following conduct involving customers or vendors should be prohibited as undesirable in any business setting:

- borrowing money from vendors or customers;
- requesting or accepting brides, kickbacks, expensive gifts or lavish entertainment from vendors or customers;
- requesting or accepting discounts on purchases fro vendors or customers that are not offered to the general public;
- blacklisting customers or vendors;

- lying to customers or vendors, misrepresenting the company's goods or services, or falsely disparaging a competitor's goods or services; and

- requiring customers to buy unwanted products in order to get products they do want.

Governmental Relations

The Code should

- prohibit "off the books" accounts or funds;

- require accurate and complete financial and other records;

- prohibit false, misleading or incomplete reports to government agencies;

- prohibit lobbying except as expressly authorized by the company; and

- require politically active employees to make clear they speak only for themselves and not for the company;

Environmental Laws

The Code should require employees to comply with all applicable environmental laws, and to report known or suspected violations to management.

One point that surely will apply to all companies is this: to be effective, the Code of Ethics must have top management's enthusiastic endorsement and adherence. A company might as well trash its Code of Ethics if the Code prohibits nepotism, for example, but the CEO is allowed to hire his son-in-law as Special Assistant to the President.

References:

Sarbanes-Oxley Act, 15 U.S.C. § 7201

Federal Sentencing Guidelines, Chapter 8

www.ussc.gov/orgguide.htm

www.ussc.gov/2004guid/RFMay04_Corp.pdf

Government Contractors' Employment Obligations

Government contractors are subject to the same workplace laws that apply to purely private-sector employers, including anti-discrimination laws, laws affording employees the right to unionize and forbidding companies from interfering with their organizing efforts, wage-and-hour laws, the Family and Medical Leave Act, health insurance continuation under COBRA, etc.

But most companies that do business with the federal government have additional obligations not applicable to other employers.

Executive Order 11246

In 1965, President Lyndon Johnson issued EO 11246. As subsequently amend-ed, EO 11246 requires all non-exempt government contracts to contain provisions by which the contractor agrees, among other things –

- not to discriminate against any employee or application for employment because of race, color, religion, sex or national origin;

- to develop a written affirmative action plan and take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex or national origin;

- to post notices of its obligations under EO 11246 in the workplace and to furnish notices to labor unions with which it has a collective bargaining agreement;

- to include an equal opportunity provision in all employment ads and postings; and

- to include all these same contract provisions in contracts with non-exempt subcontractors and vendors.

Failure to comply with these requirements subjects the contract to possible cancellation.

Within the Department of Labor, administration of EO 11246 is handled by the Office of Federal Contract Compliance Programs (OFCCP). Under authority of EO 11246, the OFCCP has exempted all contracts and subcontracts of $10,000 or less. Contractors who have fewer than 50 employees or whose contracts are for less than $50,000 are exempt from the affirmative action requirements. Prime contractors and first tier subcontractors are also exempt from certain reporting requirements.

Non-exempt government contractors are required to file an Employer Information Report, Form EEO-1 (also known as Standard Form 100), within 30 days after the award of a contract and annually by September 30 thereafter. Additional information may be required on a case-by-case basis.

Rehabilitation Act

The Rehabilitation Act of 1973 served as a model for the Americans with Disabilities Act, passed in 1990. Both laws address, in similar terms, employment discrimination against persons with disabilities. While the ADA applies to the workforce generally, the Rehabilitation Act is limited to federal contractors and subcontractors whose contracts exceed $10,000.

Veterans

The Vietnam Era Veterans' Readjustment Assistance Act of 1974 (VEVRAA) applies to federal contractors and subcontractors whose contracts exceed $10,000. VEVRAA prohibits discrimination against "special disabled veterans" and "veterans of the Vietnam era." A special disabled veteran is defined generally as a veteran who has a 30% or greater disability rating or who was released from active duty because of a service-elated disability. A Vietnam-era veteran is defined generally as a veteran (other than a veteran with a dishonorable discharge) who served in Vietnam or who served anywhere between August 1964 and May 1975.

Unions

Executive Order 13201, issued by President Bush shortly after taking office, requires inclusion of a clause in non-exempt government contracts to the effect that the contractor will post a notice (the "Beck Poster") in unionized shops informing employees that they can request a reduction in their union dues to the extent the dues are used to support activities not related to collective bargaining, contract administration, or grievance adjustment. This Executive Order does not apply to contacts of under $100,000, to contractors with fewer than 15 employees, and to contractors in right-to-work states. For more information, go to

www.dol.gov/esa/regs/compliance/olms/BeckInfo.htm

Minimum/Prevailing Wages and Overtime

The Fair Labor Standards Act imposes minimum wage and overtime requirements on employers generally. Additional laws apply to federal contractors.

The Davis-Bacon Act, applicable to federal government construction contracts in excess of $2,000, requires contracts to contain provisions requiring employers to pay "prevailing wages" for various categories of employees as determined by the Secretary of Labor. Similar prevailing wage laws apply to federal government supply contracts (the Walsh-Healey Public Contracts Act) and to federal government service contracts (the McNamara-O'Hara Service Contract Act).

In general, an employer's obligation to pay a premium for overtime – time-and-one-half for hours worked in excess of the standard 40-hour workweek – is determined under the Fair Labor Standards Act, just as it is for purely private-sector employers. However, the Contract Work Hours and Safety Standards Act, which applies to virtually all federal government contracts in excess of $100,000, requires employers to pay their laborers and mechanics (defined to include watchmen, guards, apprentices, trainees, helpers firefighters, fireguards and workers performing dredging or rock excavation in any river or harbor) time-and-one-half for overtime. Since the overtime exemptions under the Contract Work Hours and Safety Standards Act are different from those under the Fair Labor Standards Act, it is possible that an otherwise exempt employee will be entitled to overtime for work done under a government contract.

Government contracting agencies must include appropriate clauses in their contracts implementing applicable statutory requirements. The Federal Procurement Regulations contain a standard set of contract clauses, available electronically at:

www.arnet.gov/far/current/html/52_222.html

The Department of Labor's Federal Contract Compliance Manual is available for download at

www.dol.gov/esa/regs/compliance/ofccp/fccm/fccmanul.htm

References:

Rehabilitation Act, 29 U.S.C. § 793
Vietnam Era Veterans' Readjustment Assistance Act, 38 U.S.C. § 4212
Davis-Bacon Act, 40 U.S.C.A. § 3141
Walsh-Healey Public Contracts Act, 41 U.S.C. § 35
McNamara-O'Hara Service Contract Act, 41 U.S.C. § 351
Contract Work Hours and Safety Standards Act, 40 U.S.C. § 3701
Federal Acquisition Regulations, 48 C.F.R. § 22.300

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In this issue of EMPLOYER ALERTS! . . .

- Tax Law Changes Could Promote Employee Claims
- Should Your Company Have a Code of Ethics?
- Government Contractors' Employment Obligations

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.
7700 Old Georgetown Road, Suite 800
Bethesda, MD 20814

Employer ALERTS!

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By Charles H. Fleischer, Esq.

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.

Maryland Courts May Not Second-Guess Good Faith Firing

Most employment relationships are "at will," meaning that the employee can quit or be fired at any time, for any reason (except an illegal reason, such as discrimination) or for no reason at all. In other words, an employee does not need a good reason to quit, and the employer does not need good cause to fire. In at-will situations, an employer can even act arbitrarily or unfairly, although doing so is hardly good business practice.

But what if the employee has a contract for, say, a term of three years, which states that during the three-year term the employee can only be fired for good cause? Is the employer's determination of good cause subject to second-guessing by a court or jury? Suppose, for example, that an employer discovers valuable company property missing from an area in which only employees have access. The employer conducts a thorough, impartial investigation and, based on that investigation, concludes that a particular employee, who has a contract of employment, is responsible. If the employee is then fired for good cause, does the employee have a right to try to prove in court that he didn't steel the property? In other words, are juries "super personnel officers" authorized to second-guess an employer's decision?

Courts in other jurisdictions have ruled that, so long as the employer has acted reasonably and in good faith, an employee cannot challenge the employer's factual findings in court. As the Wyoming Supreme Court ruled in a 2003 decision, the question is not, Did the employee in fact commit the act leading to termination? Rather, the question is, Was the factual basis on which the employer concluded a dischargeable act had been committed reached honestly, after an appropriate investigation and for reasons that are not arbitrary or pretextual? See "When Does Employer Have Cause for Termination?", EMPLOYER ALERTS!, May 2003, p. 4.

Maryland's highest court has now reached the same conclusion, holding that an employer's good faith factual determination of whether good cause exists cannot be second-guessed by a jury. Instead, the jury is limited to deciding whether the employer acted arbitrarily or relied on facts not reasonably believed to be true.

The Maryland case involved an employee of Towson University named Michael Conte, who in 1996 was appointed to head an economics institute maintained by the University. His appointment was for 39 months under a contract which prohibited the University from firing him except for cause. Part way through his term, the University became aware of accounting irregularities in the institute which jeopardized a contract the institute had with the Maryland Department of Human Resources. The University was able to save its DHR contract, but it lost confidence in Conte's management. Further audits revealed additional irregularities and eventually Conte was fired.

Conte sued in Baltimore County Circuit Court for breach of contract and the jury found in his favor, awarding him $926,822 in damages. On appeal, the Maryland Court of Appeals reversed and ruled in favor of the University. The appeals court found that Conte's contract was ambiguous as to whether the fact-finding prerogative lay with the University. Nevertheless, viewing the contract as a whole, the Court concluded that the University retained this fact-finding prerogative and, so long as the University acted reasonably and in good faith, its finding of cause to fire Conte must be upheld.

While the decision is certainly gratifying, employers should take note that whenever they enter into contracts requiring termination for cause, the contract should specify just how cause is to be determined. A contract phrase such as, "The employer, in its reasonable discretion, may determines what constitutes good cause" will probably do the trick.

References: *Life Care Centers of America, v. Dexter*, 65 P.3d 385 (Wyo. 2003); *Towson Univ. v. Conte*, 2004 WL 2599598 (Md. 2004).

Meaning of "Wages" Under Maryland's Treble Damage Law

In another important Maryland decision, this one by the Court of Special Appeals (Maryland's intermediate appellate court), severance payments were held not to constitute "wages" under Maryland's Wage Payment Act, even though the employer was contractually obligated to make the payments. Had the payments been deemed wages, the employer could have been hit with treble damages for failure to pay. See "*More on Treble Damages in Maryland,*" EMPLOYER ALERTS!, Jan. 2002, p. 5

Diane Stevenson was a Senior Vice President with Federal Bancorp at the time of its 1998 merger with BB&T. BB&T offered Stevenson a similar position after the merger, under a three-year contract which allowed BB&T to terminate her for cause. The contract also allowed termination without cause, but in that case BB&T had to pay Stevenson "termination compensation" equal to one year's earnings. Termination compensation would also be due in the event Stevenson resigned, but in a lesser amount based on the time remaining under her contract. Both types of termination compensation were conditioned on Stevenson's complying with the non-compete provisions of the contract.

In 1999 BB&T decided to replace Stevenson. However, when it calculated her termination compensation, it used the formula applicable to voluntary quits, and it also disregarded Stevenson's earnings from stock options. So Stevenson sued, claiming entitlement to an additional $314,884 in termination compensation, and claiming further that the amount should be trebled under the Wage Payment Act.

The court started its analysis with the Wage Payment Act itself, which defines "wage" as "all compensation that is due to an employee for employment," including bonuses, commissions, fringe benefits, and "any other remuneration promised for service." The Court rejected BB&T's argument that since termination pay is not expressly mentioned in the Act, it cannot be a wage. The Court also rejected BB&T's alternative argument that severance pay can never be remuneration for an employee's services, saying that severance pay that is based on the length or nature of an employee's service is covered by the Act.

Here, however, Stevenson's termination compensation was not based on past service, but was instead tied to her not competing with BB&T after termination. Therefore, Stevenson was not entitled to treble damages based on improper payment of termination compensation.

Since the case had to go back to the trial court for other reasons, the Court of Special Appeals took the opportunity to clarify an open question under the Wage Payment Act. The Act gives the employee a right to sue for unpaid wages and, as noted above, it allows the court to award treble damages, unless the employer withheld wages based on a bona fide dispute. The trial court in this case had awarded both wages and treble damages, in effect ordering *quadruple* damages. The appellate court found this to be error, saying that the maximum an employee could recover is three times the wrongfully withheld wages.

References: Md. Code, L&E §§ 3-501, et seq.; *Stevenson v. Branch Banking & Trust Corp.*, 2004 WL 2601132 (Md.App. 2004).

Male Guards Barred From Michigan Women's Prison

Title VII of the federal Civil Rights Act makes it an unlawful employment practice to discriminate against any individual because of such individual's race, color, religion, sex, or national origin. Title VII has an exception, however, for bona fide occupational qualifications (BFOQs):

> It shall not be an unlawful employment practice for an employer to hire and employ employees ... on the basis of his religion, sex, or national origin in those certain instances where religion, sex, or national origin is a bona fide occupational qualification reasonably necessary to the normal operation of that particular business or enterprise.

Note that the BFOQ exception applies only to religion, sex and national origin. It does not permit discrimination on the basis of race or color, regardless of the circumstances.

The question recently before a federal appeals court was whether a correctional facility in Michigan could use sex as a BFOQ for guards who closely supervised female inmates. The Michigan prison system apparently had a long history of abusing its female prisoners. Back in 1994 the Civil Rights Division of the U.S. Department of Justice investigated and found sexual abuse by guards, including rape and other sexual assaults, fondling of inmates during pat-down searches, sexually suggestive comments, and surveillance while prisoners were undressing and using shower and toilet facilities.

The Department of Justice filed suit against the state of Michigan, alleging that the state was violating the prisoners' constitutional rights by failing to protect them from sexual misconduct and unlawful invasions of their privacy. That suit ended in a settlement agreement in which Michigan pledged to minimize access to secluded areas and one-on-one contact between male guards and female inmates, to implement a "knock and announce" policy by which male guards were required to announce their presence before entering into areas where female prisoners were likely to be in a state of undress, and to restrict pat-down searches by male guards.

> To implement the settlement agreement, prison authorities changed the classification of some 267 guard positions to "female only." That change prompted a group of guards, both male and female, to sue for sex discrimination under Title VII, claiming that gender was not a BFOQ in this case.

The trial court agreed with the guards that gender was not a BFOQ here, but the U.S. Court of Appeals for the Sixth Circuit reversed. The appeals court recognized that the employer bears the burden of showing the necessity of gender discrimination. Further, the discrimination must have a basis in fact, must be reasonably necessary (not just convenient) to the operation of the employer's business, and there must be no reasonable alternatives to discrimination. Here, the employer met its burden by showing that the gender restriction would reduce the likelihood of further sexual misconduct, it would remove gun-shy male guards who avoided proactive surveillance out of fear of being accused of sexual misconduct, it would permit increased monitoring of prisoners, and it would reduce the incidence of false accusations of abuse.

References: 42 U.S.C. § 2000e; *Everson v. Michigan Dept. of Corrections*, 2004 WL 2753189 (6th Cir. 2004).

Dress Code Trumps Duty of Religious Accommodation

Under Title VII, religion, along with race, color, sex and national origin, is one of the factors an employer generally cannot consider when making workplace decisions. But religion is also specially defined in Title VII to include

all aspects of religious observance and practice, as well as belief, unless an employer demonstrates that he is unable to reasonably accommodate to an employee's or prospective employee's religious observance or practice without undue hardship on the conduct of the employer's business.

A recent federal appeals court decision confirms that the employer's duty to accommodate an employee's religious observance or practice is fairly limited.

When Costco hired Kimberly Cloutier to work at its Springfield, Massachusetts store, she sported multiple earrings and four tattoos. Over the next two years, she engaged in various forms of additional body modification, including facial piercing and cutting. When Costco updated its dress code to prohibit all facial jewelry except earrings and attempted to enforce the code against Cloutier, Cloutier responded that she was a member of the Church of Body Modification (an Internet-based organization) and that her facial piercings were part of her religion.

In support of her claim, Cloutier provided Costco with information from the church's website stating the church's mission was to promote its members' growth as individuals through body modification. Costco reviewed the information, but nevertheless insisted that Cloutier remove here eyebrow rings while at work. Cloutier refused, claiming that even replacing the rings with plastic retainers or covering them with a flesh-colored bandage would contravene her religious convictions. According to Cloutier, the only accommodation acceptable to her would be exempting her from the dress code. Costco, on the other hand, argued that such an exemption would create an undue hardship because it would interfere with its ability to maintain a professional appearance.

Cloutier was eventually fired, and she then sued for religious discrimination.

The U.S. Court of Appeals for the First Circuit agreed with Costco that the accommodation Cloutier insisted upon – an exemption from the dress code – would create an undue hardship. Relying on an earlier Supreme Court case, the court said that an accommodation which imposes anything more than minimal cost on an employer is an undue hardship. "Cost" in this context is not limited to economic cost, such as lost business or having to hire additional employees to cover a Sabbath observer, but also includes non-economic cost such as compromising the integrity of a seniority system.

Here, Costco had a legitimate interest in presenting to its customers a workforce that was reasonably professional in appearance. Granting to Cloutier the only accommodation she would accept would be an undue hardship because it would adversely affect the employer's image. Costco's determination that facial piercings detract from the neat, clean and professional image Costco aims to cultivate was within Costco's business discretion, said the court.

References: 42 U.S.C. § 2000e; *Cloutier v. Costco Wholesale Corp.*, 2004 WL 2731496 (1st Cir. 2004); *Trans World Airlines, Inc. v. Hardison,* 432 U.S. 63 (1977).

Deputy Sheriff's Mental Disorder Posed Direct Threat

Like religious discrimination under Title VII, disability discrimination under the Americans With Disabilities Act also includes a duty of reasonable accommodation. But unlike Title VII, the ADA allows an employer to require that an individual not pose a direct threat to the health or safety of the individual himself or others in the workplace that cannot be eliminated by reasonable accommodation.

A recent federal case arising in Wyoming illustrates how the direct threat defense works.

Deputy Sheriff Lorraine McKenzie worked in the Casper, Wyoming sheriff's office for ten years, reaching the rank of sergeant. In the mid-1990s she began suffering from a variety of psychological afflictions, including post traumatic stress disorder (PTSD) as a result of childhood abuse by her father.

At one point, McKenzie fired six rounds from her revolver into the ground at her father's grave. She was immediately suspended and told she would have to undergo psychological evaluation before she could return to duty. Shortly thereafter, her psychiatrist wrote to the sheriff's office stating that McKenzie's return to her position might be hazardous to herself and the public, and that further extensive evaluation would be necessary. When McKenzie's accrued leave had been exhausted, she voluntarily resigned to seek additional care. In the weeks that followed, she suffered serious self-inflicted wounds and drug overdoses requiring hospitalization.

After a course of medication and therapy, McKenzie applied for return to her previous position. The sheriff's office rejected her, however, due to her past medical history. That rejection prompted McKenzie to sue for disability discrimination under the ADA.

At trial, McKenzie's psychiatrist testified that she was unable to certify McKenzie as able to return to her prior position because she (the psychiatrist) was not familiar with McKenzie's duties. The psychiatrist further testified that PTSD is an episodic/crisis type condition, where there are peaks and valleys and no way to predict when McKenzie might experience problems again. The psychiatrist also said that there are no guarantees McKenzie could return to work.

The jury found that McKenzie was disabled within the meaning of the ADA, and that the sheriff's office had rejected her application based on her disability. The jury also found, however, that McKenzie posed a direct threat to herself or other officers and she therefore was not qualified to be a deputy. The appellate court affirmed, noting that in situations where, as here, the job in question implicates the safety of others, the candidate for employment has the burden of proving that she does not pose a direct threat. The jury in this case was justified in finding that McKenzie had not met her burden.

References: 42 U.S.C. § 12101; *McKenzie v. Benton*, 2004 WL 2526450 (10th Cir. 2004).

NLRB Reverses Itself (Yet Again) on Presence of Co-Worker

Absent a union, an employer is generally free to deal with his employees on an individual basis. However, Section 7 of the National Labor Relations Act gives all employees, including non-union employees, the right to engage in "concerted activities for the purpose of collective bargaining or other mutual aid or protection."

In 1975 the Supreme Court upheld a National Labor Relations Board ruling that Section 7 of the Act gives a union employee, at the employee's request, the right to have a union representative present at an interview in connection with an investigation that the employee reasonably believes may result in disciplinary action against the employee.

Since 1975, the Board has flip-flopped on whether Section 7 also gives non-union employees the same right. In a 1982 case, the Board ruled that non-union employees could insist upon the presence of a co-worker. In 1985, the Board reversed itself and denied any such right to non-union employees. And in a 2000 decision, the Board reversed itself again, granting to non-union employees the same right as union employees to have a co-worker or representative present at an interview that relates to a disciplinary matter. See "Non-Union Worker's Right to Witness at Disciplinary Hearing," EMPLOYER ALERTS!, Aug. 2000, p. 2.

In yet another reversal, the Board has now ruled that non-union employees do not have a right to have a co-worker present during a disciplinary interview. The Board reasoned that the National Labor Relations Act could fairly be interpreted either way – as allowing or denying non-union workers the same representational rights as union workers. Therefore, it was up to the Board to determine which rule to adopt in furtherance of national labor relations policy. And as a policy matter, the Board concluded that granting the right to an employee in a non-union setting impairs, rather than furthers, workplace labor relations.

References: 29 U.S.C. § 151; *NLRB v. Weingarten, Inc.*, 420 U.S. 21 (1975); *Materials Research Corp.*, 262 NLRB 1010 (1982); *Sears, Roebuck & Co.*, 274 NLRB 230 (1985); *E.I. DuPont & Co.*, 289 NLRB 627 (1988); *Epilepsy Foundation of Northeast Ohio,* 331 NLRB 676 (2000), aff'd, 268 F.3d 1095 (D.C.Cir. 2001); *IBM Corp.*, 341 NLRB No. 148 (2004).

New IRS Rulings

The IRS recently issued rulings on the following subjects of interest to employers:

Signing bonuses

When an employer pays a signing bonus to a new employee, the amount of the payment is treated the same as wages for work done. This means the employer must withhold federal income tax and include the payment for FICA and FUTA purposes. The amount must also be reflected in the W-2 issued to the employee at year's end.

Reference: Rev. Rul. 2004-109.

Contract cancellation payments

Suppose employer and employee enter into a three-year contract, but after a year or so the parties recognize that the arrangement isn't working. So they agree that the employer will pay a lump sum to the employee in exchange for early cancellation of the contract. How is that payment treated? As with signing bonuses, the payment is treated just like wages for FICA, FUTA and income tax withholding purposes.

Reference: Rev. Rul. 2004-110.

Threshold for FUTA deposits

Existing regulations generally require employers to deposit FUTA taxes quarterly, but an exemption provides that an employer is not required to make a deposit until the accumulated tax liability exceeds $100. Effective December 1, 2004, the $100 threshold has been raised to $500.

Reference: T.D. 9162.

Standard mileage rate deductions

The IRS looks at the standard mileage rate deduction every year and changes the rate as appropriate. Beginning in 2005 the standard deduction for business use of an automobile will be 40.5 cents per mile (up from 37.5 cents). Lower rates apply to charitable, medical and moving expense deductions relating to automobile use. Since many employers reimburse their employees based on this standard rate, reimbursements will be going up in 2005 as well. Although the standard date is intended to cover actual automobile expenses (gasoline, maintenance and repairs, depreciation, etc.), taxpayers may, if they wish, deduct their actual expenses provided the expenses are properly substantiated.

Reference: Rev. Proc. 2004-64.

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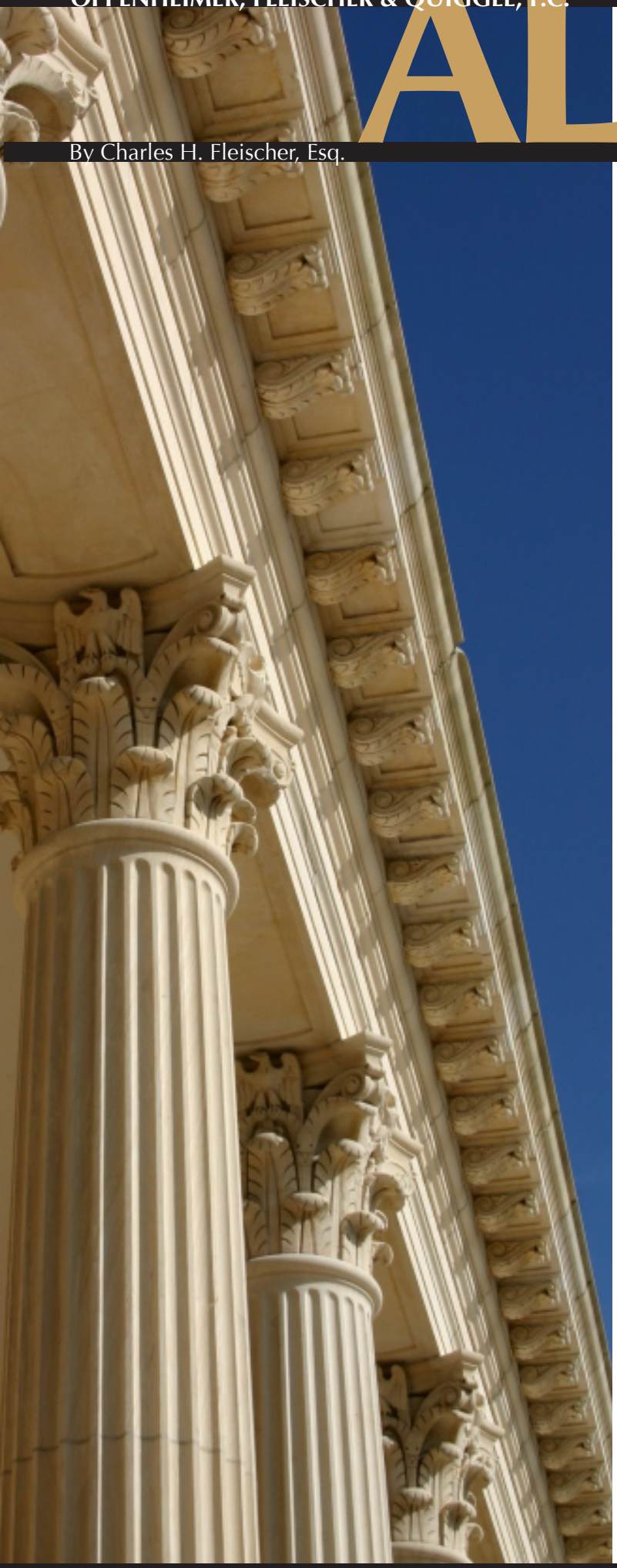
Employer ALERTS!

By Charles H. Fleischer, Esq.

Spring 2005 – Volume V, No. 4



When the Boss's Lover Gets Promoted Do Others Suffer Sex Discrimination?

Suppose a supervisor who is romantically involved with a subordinate promotes the subordinate, or gives the subordinate a raise or desirable job assignment. Can other employees who are equally qualified but who do not have personal relationships with the supervisor claim sex discrimination? The Equal Employment Opportunity Commission's guidelines on sex discrimination say yes and at least one court agrees. In a 2003 case the federal trial court in Oregon ruled that a female candidate for employment who lost out on getting a job to another woman who, at the time, was sleeping with a member of the interview panel, could make just such a claim.

Now the U.S. Court of Appeals for the Seventh Circuit, which sits in Chicago, has rejected the notion that favoritism toward a paramour amounts to sex discrimination against others.

Jay Preston, a dentist, was the long-time director of the dental clinic within the Wisconsin Health Fund. The Fund was operating at substantial losses and the dental clinic itself lost $1 million in 1999. Preston, who held an MBA degree as well as a dental degree, presented the Fund's CEO, Bruce Trojak, with a well-developed and thoughtful business plan to stem the financial losses. Trojak fired Preston anyway, claiming the business plan was too little, too late. Trojak replaced Preston with a much younger female named Linda Hamilton.

Preston sued for sex discrimination, claiming that Hamilton had no credentials for the job except eagerness, and that the reason he was replaced by Hamilton was that Trojak and Hamilton were having an affair. Although Trojak denied that he and Hamilton were romantically involved, the Court characterized Trojak's testimony as "not terribly credible."

Assuming for purposes of its opinion that Hamilton was hired because of her involvement with Trojak, the Seventh Circuit nevertheless rejected Preston's suit. The Court held that a male executive's romantically motivated favoritism toward a female subordinate is not sex discrimination, even when it disadvantages a male competitor of the woman. To prove its point, the Court pointed out that, under Preston's theory, Preston would have been fired to make way for Hamilton even if Preston had been a woman. In other words, Trojak's actions were not motivated by discriminatory animus against men – which *would* be sex discrimination – but instead by a desire to favor a particular woman with whom he was involved.

References: 42 U.S.C. § 2000e (Title VII); 29 C.F.R. § 1604.11(g); *Prowell v. Oregon*, 2003 WL 23537979 (D.Or. 2003); *Preston v. Wisconsin Health Fund*, 397 F.3d 539 (7th Cir. 2005).

Medical Exams and Conditional Offers of Employment

The Americans With Disabilities Act has special rules for medical examinations. Prior to actually offering employment, an employer may never require an applicant to undergo a medical exam (except a test for illegal drugs, which is not considered a medical exam). The ADA recognizes, however, that an employer may need to conduct medical exams for certain reasons, such as assuring that a prospective employee can perform the job safely and effectively. Therefore, once the employer actually offers employment, he may condition the offer on the results of a medical exam *if* –

- all entering employees in the job category are subject to examination;
- the exam requirement can be shown to be job-related and consistent with business necessity;
- the resulting medical information is separately maintained and treated as confidential; and
- the results are not used to discriminate against persons with disabilities.

As American Airlines recently learned, an offer of employment in these circumstances may be conditioned *only* on passing the medical exam. If the offer is conditioned on any additional pre-employment requirements, the medical exam is illegal.

At various times during the late 1990s, a number of individuals who were HIV-positive and receiving medical treatment for that condition applied to American Airlines to become flight attendants. They first responded to telephone surveys conducted by the company, and then provided more detailed information in written application forms. Based on these initial screenings, the company flew them to Dallas for in-person interviews.

Upon completing the Dallas interviews, the applicants were given written offers of employment, conditioned on passing a drug test, a medical examination, and a background check. Since the applicants were then physically present in Dallas, the company as a convenience directed the applicants to proceed to the company's medical department for the medical exams.

As part of the medical examination procedure, the applicants were required to complete medical history forms that asked about any medications they were taking and asked whether they had any of a long list of medical conditions, including HIV and AIDS. In each case, the applicants denied having HIV or AIDS and failed to disclose related medications they were taking. They were also interviewed by nursing personnel and again omitted mention of their conditions and treatment.

At some point during the examination procedure, the nurses drew blood from the applicants and submitted the samples for testing. Blood tests revealed anomalies which did not fit with the applicants' medical conditions as reported on their medical forms, so the medical department wrote to the applicants and requested explanations. In each case, the applicants then disclosed their HIV-positive status and medications.

On receipt of this additional information, the medical department informed the company that the applicants did not meet company medical guidelines due to "nondisclosure," without saying what the specific undisclosed matters were. The company then wrote to the applicants rescinding the conditional offers of employment on the grounds that they had failed to provide full and correct information.

In the applicants' subsequent lawsuit against American Airlines, the federal Court of Appeals for the Ninth Circuit observed that the ADA establishes a two-step process for employers who require medical exams. The first step is a conditional offer of employment and the second is the medical exam. By isolating the medical exam from other requirements, said the Court, an applicant can more easily determine whether employment was denied for a reason which might amount to unlawful discrimination under the ADA. In other words, the medical exam must come last, after all other requirements and conditions have been satisfied; an offer of employment that is conditioned on passing a medical exam must be conditioned *only* on the medical exam and nothing else.

Here American Airlines conditioned its offers on satisfactory background checks and drug tests as well as medical exams. To conduct a medical exam under these circumstances, before other requirements have been satisfied, violates the ADA, ruled the Court.

References: 42 U.S.C. §12101; *Leonel v. American Airlines, Inc.*, 2005 WL 502874 (9th Cir. 2005).

Alcoholism as a Disability Under the ADA

William Moorer worked for the Baptist Memorial Health Care System for 17 years prior to his termination. Over that period he enjoyed a number of promotions, rising to administrator of two of the Health Care System's hospitals. In a January 1997 evaluation his supervisor identified some performance concerns and met with him to discuss those concerns. As a result of that meeting, Moorer and his supervisor developed a plan of action for improvement.

In a later reorganization, Moorer began reporting to a new supervisor, Cathy Hill. Moorer's previous supervisor told Hill about the earlier performance concerns and said that Moorer had made progress in some areas but not others. He suggested that Hill follow up on those other areas.

Hill did follow up, informing Hill in July 1997 that certain deficiencies still needed correction and that failure to improve his overall job performance by mid-September might result in termination.

Later that same month, while Hill and Moorer were attending a meeting, Hill thought she detected alcohol on Moorer's breath. Hill also noticed his ruddy complexion and observed him slump in his chair and act fidgety. Hill did not confront Moorer about possible alcohol abuse, but instead informed higher management of her suspicions. At management's suggestion, Hill contacted the Health Care System's employee assistance program (EAP) and described the situation. In consultation with EAP personnel, Hill referred Moorer to the EAP for a mandatory fitness-for-duty evaluation. In the process, Hill told Moorer that she had a family history of alcoholism and that she thought Moorer was an alcoholic. Hill also called Moorer's wife and told her about Hill's own family history of alcoholism, describing the condition as an incurable and deadly disease. Moorer went for the required evaluation and was diagnosed as having a substance abuse problem. On the advice of EAP personnel, Moorer underwent a five-week course of in-patient treatment beginning in late August.

While Moorer was undergoing treatment, Hill decided to fire him. According to Moorer, during the firing process Hill told Moorer that his work problems were caused by his alcoholism.

Dress Codes and Discrimination

Moorer sued for discrimination under the Americans With Disabilities Act in a Tennessee federal court, claiming that he was terminated because of his disease. Hill countered that the termination was due to performance problems, but the court did not believe her. Accepting Moorer's version of the facts as true, the court awarded Moorer over $1 million in damages. On appeal, the Court of Appeals for the Sixth Circuit upheld the trial court, explaining that the ADA protects individuals with disabilities who, with or without reasonable accommodation, can perform the essential functions of the jobs they hold or are applying for. For ADA purposes, a person is "disabled" if he or she

- *has* a physical or mental impairment that substantially limits one or more major life activities, such as caring for oneself, performing manual tasks, walking, seeing, hearing, speaking, breathing, learning, and working;
- *has a record* of such an impairment; or
- *is regarded* as having such an impairment.

According to the appeals court, Moorer was *regarded* by his employer as being substantially limited in his ability to work due to alcoholism. His termination due to alcoholism therefore violated the ADA.

What could the employer have done in this case to avoid Moorer's successful claim? First, it should have allowed him to finish his treatment course and return to work. Further, if Moorer requested accommodation for alcoholism, such as being allowed periodic leave to attend Alcoholics Anonymous meetings, the employer would have to engage is good faith discussions with him to determine whether such an accommodation was reasonable. Once he was back at work, the employer would have every right to monitor his performance, identify any continuing shortcomings, and take appropriate disciplinary action based on those shortcomings. The employer could also enforce any rules it might have regarding being under the influence of alcohol while at work. What the employer couldn't do was fire Moorer simply because it regarded him as an alcoholic.

References: 42 U.S.C. § 12101; 29 C.F.R. § 1615.103; *Moorer v. Baptist Memorial Health Care System,* 398 F.3d 469 (6th Cir. 2005).

Dress codes are common in the workplace, but they are sometimes viewed as discriminatory. See, for example, the article in last quarter's issue, "Dress Code Trumps Duty of Religious Accommodation," EMPLOYER ALERTS!, Winter 2005, p. 4, discussing a case of a Costco employee who claimed her employer's rule against facial piercings violated her rights as a member of the Church of Body Modification. See also "Dress Codes and Sex Discrimination," EMPLOYER ALERTS!, July 2000, p. 3; "Do Females Have Constitutional Right to Wear Skirts," EMPLOYER ALERTS!, March 2003, p. 6;

This article deals with two related issues – whether an employer may require its female employees who serve the public to wear makeup, and whether a company can enter into a collective bargaining agreement with its union that requires employees to wear a uniform bearing the union's logo.

Makeup

Darlene Jaspersen was a bartender for Harrah's Casino in Reno, Nevada. She had an outstanding record and repeatedly received positive feedback on her excellent service and good attitude. When Harrah's adopted a policy of requiring all its female beverage servers to wear makeup, including foundation or powder, blush, mascara and lipstick, Jaspersen objected, saying that it "forced her to be feminine" and made her feel "dolled up" like a sex object. Harrah's also adopted dress and grooming standards for male beverage servers which among other things *prohibited* facial makeup.

Harrah's told Jaspersen that the new requirements were mandatory for all beverage servers, and it gave her 30 days to apply for another position that did not have the makeup requirement. At the expiration of 30 days, Jaspersen had not applied for another job, so she was terminated.

In her subsequent sex discrimination suit, the Court of Appeals for the Ninth Circuit ruled that having different dress and grooming standards for men and women is not sex discrimination. The Court noted that if Jaspersen had shown the grooming standards imposed a greater burden on women than on men, she might have been able to make out a good discrimination claim, but here she failed to offer any such evidence.

References: 42 U.S.C. § 2000e (Title VII); *Jespersen v. Harrah's Operating Co.*, 392 F.3d 1076 (9th Cir. 2004).

Union Insignia

BellSouth and the Communications Workers of America have had a collective bargaining relationship since the 1940s. The union contract in force during the mid-1990s contained a requirement that employees in telecommunications and those who had contact with the public wear a uniform bearing both the company logo and the union logo.

Two non-union employees, whose job classifications required them to wear uniforms with the company and union logos, objected. They pointed to a provision of the National Labor Relations Act which not only gives employees the right to "engage in ... concerted activities for the purpose of collective bargaining," it also gives employees the right to "refrain from any and all such activities."

The National Labor Relations Board upheld the uniform requirement, but the Court of Appeals for the Fourth Circuit, headquartered in Richmond, disagreed. The Court said that the requirement interferes with employees' rights to refrain from union activity. And while a union, when negotiating with management, can bargain away an employee's economic rights, it cannot bargain away an employee's right to participate (or not to participate) in union activities.

References: 29 U.S.C. § 157; *Lee v. N.L.R.B.*, 393 F.3d 491 (4th Cir. 2005).

Discrimination on the Basis of Credit

The word "discrimination" is usually thought of as involving characteristics such as race, national origin, gender, religion, etc. But there are other ways in which an employer can be guilty of discrimination. One of them as to do with an employee's or applicant's financial status.

Employee Bankruptcy

The federal Bankruptcy Code prohibits an employer from discriminating against an individual solely because that individual has filed for bankruptcy protection, has been insolvent before or during the pendency of a bankruptcy case, or has failed to pay a debt that is dischargeable in bankruptcy. The qualification "solely" is important here, as illustrated in a recent case before the U.S. Court of Appeals for the Sixth Circuit.

William and Shirley White, husband and wife, both worked for Kentuckiana Livestock Market in Kentucky. William was the company's secretary-treasurer and bookkeeper; Shirley was a secretary there. Three days after notice was published in a local newspaper that they had jointly filed for bankruptcy they were both fired. They both then sued to contest the firings as illegal under the Bankruptcy Code.

At trial there was evidence showing that William had previously borrowed money to invest in a welding and fabricating shop and, when he was unable to repay the loan, had to declare bankruptcy. Because of the bankruptcy, William had to surrender his personal automobile. William then asked his employer to furnish him with a company car. In exchange, William promised to help company officials cheat on their taxes by not reporting commissions they received.

During the trial the company gave a variety of reasons for firing William, including sloppy bookkeeping and poor customer and employee relations, as well as the offer to falsify tax returns. It was clear, however, that the bankruptcy was at least one of the reasons for William's termination. Shirley was terminated simply because she was William's husband.

On this evidence, the trial rejected the Whites' claim and the Court of Appeals agreed. It said that "solely" means exactly that. Where, as here, non-bankruptcy reasons were part of the company's motivation, the Whites had no basis to contest the firings under the Bankruptcy Code.

References: 11 U.S.C. § 525; *White v. Kentuckiana Livestock Mkt., Inc.*, 397 F.3d 420 (6th Cir. 2005).

Wage Garnishments

Federal law makes it illegal to discharge an employee who is subject to garnishment for any one indebtedness. Similar restrictions apply to employees who are subject to tax levies, U.S. Department of Education garnishments for repayment of student loans, and withholding orders in connection with family support obligations.

References: 15 U.S.C. § 1671; 20 U.S.C. § 1095a; 42 U.S.C. § 666; 29 C.F.R. § 870.

Defamation Based on Intra-Company Communications

Defamation is usually defined as the publishing of a false statement of fact that tends to injure a person's reputation and good name. A false statement is "published" when it is transmitted to some third person, either orally or in writing. Even when a false and damaging statement is published, however, it may not be grounds for a lawsuit if it is "privileged," meaning that the speaker or writer is protected from suit because of special circumstances surrounding the making of the statement.

In the context of defamation, privileges come in two types – absolute and conditional. For example, when a congressman makes a statement on the floor of the House or Senate, his words are absolutely privileged, no matter how malicious his or her comments may be. In the workplace, however, an employer's statement about an employee or former employee enjoys only a conditional privilege, so that if the statement is made with malice or spite, if it lacks a legitimate business purpose, or if it is published to a wider audience than is necessary, the employer may be exposed to a defamation suit.

Suppose an employee is fired based on the employer's honest (but mistaken) belief that the employee stole money from the company. When the employee then seeks work elsewhere and the prospective new employer calls the old employer for a reference, the old employer's statement that the employee is a thief will generally be considered privileged by the courts. This is so because the old employer honestly believes the statement to be true, he has a legitimate business reason for making the statement, and he limits the publication just to the prospective new employer.

Some states have adopted statutes protecting employers in this situation. A Maryland law, for example, says that an employer, acting in good faith, may not be held liable for disclosing information about job performance of an employee or former employee to a prospective employer, if requested to do so by the employee or the prospective employer. The statute goes on to says that the employer is presumed to be acting in good faith unless it is shown by clear and convincing evidence (a higher standard than the one usually applied in civil cases) that the employer acted with actual malice or that he intentionally or recklessly disclosed false information.

But what about communications within the company – say by an employee's supervisor to higher management or by an entry in a personnel file? Are they protected by a conditional privilege? Are such communications even considered as "published," since they are transmitted only within the company itself? A handful of cases have dealt with this issue and they reach different conclusions.

Gambardella v. Apple Health Care

A recent case involved a nursing facility in Waterbury, Connecticut. An admissions coordinator at the facility had been helpful in obtaining admission of a 95-year-old woman. The woman died only three days later and, according to the admissions coordinator, the woman's niece gave the coordinator her aunt's personal belongings as a gesture of thanks. Believing that the belongings had actually been given to the facility itself, the coordinator's supervisor fired the coordinator upon finding her removing the belongings. In the process, the supervisor made a note in the coordinator's personnel file and told higher management that the coordinator was fired for theft.

An intermediate appellate court ruled that the admissions coordinator stated a good defamation claim. The court concluded that even though the supervisor's communication stayed entirely within the company that ran the facility, it satisfied the publication requirement. Surprisingly, the court did not mention the issue of whether the communication was privileged.

Hirschfeld v. Institutional Investor

New York takes a different approach. In a 1999 decision, a terminated employee asked her supervisor to write a letter of reference, which the supervisor prepared and gave to a typist, who then typed and mailed the letter to the employee. Although the court's opinion doesn't discuss the contents of the letter, apparently it contained statements that the employee viewed as defamatory. The court denied the employee's defamation claim, however, ruling that such intra-company communications are privileged absent specific proof of malice. The court also ruled that the employee consented to publication by requesting the letter.

Schrader v. Eli Lilly & Co.

Eli Lilly became aware of a theft problem at its warehouse in Indiana and conducted an investigation. At the conclusion of the investigation it fired a number of employees. The company's actions spurred widespread rumors and poor morale at the warehouse. To quell the rumors and restore morale, the company developed a slide show which it presented to management at the warehouse. The slide show named the fired employees, it give the reason for termination as "loss of confidence," and it went on to emphasize the company's core values of trust and honesty.

One of the managers present at the slide show took notes (omitting the fired employees' names) and had the notes typed and posted on a company bulletin board. The bulletin board posting was accessible to some 1500 employees, as well as approximately 500 non-employee visitors.

In the fired employees' subsequent defamation action, the Indiana Supreme Court ruled that communications transmitted within the company were "published" for defamation law purposes, but they were also subject to a conditional privilege. In this case, said the Court, the communications served a legitimate company purpose. In addition, the extent of publication was not excessive under the circumstances. Therefore, the employees could not pursue their defamation claims.

References: *Gambardella v. Apple Health Care, Inc.*, 863 A.2d 735 (Conn. App. 2005); *Hirschfeld v. Institutional Investor, Inc.*, 688 N.Y.S.2d 31 (App. Div. 1999); *Schrader v. Eli Lilly & Co.*, 639 N.E.2d 258 (Ind. 1994).

OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.
7700 Old Georgetown Road, Suite 800, Bethesda, MD 20814
T: 301-656-5700 F: 301.951-0555
www.OFQ Law.com

Shortening the Time to File Workplace Lawsuits

The law generally discourages the filing of stale claims – claims that are so old that they cannot be properly pursued or defended because of faded witness memories or lost or destroyed documents. The law accomplishes this by imposing deadlines, called Statutes of Limitations, on when claims can be brought.

Workplace legal claims are no exception. For example, state law may require that a wrongful discharge suit be filed within, say, three years of the termination. A charge of discrimination under Title VII of the federal Civil Rights Act must be filed with the Equal Employment Opportunity Commission within 180 days of the discrimination (which is extended to 300 days for jurisdictions that have a state or local Fair Employment Practices Agency).

Recently the U.S. Court of Appeals for the Sixth Circuit, which sits in Cincinnati, gave employers an important new way to limit the time they are exposed to workplace claims.

When Connie Thurman applied to work for Chrysler (now DaimlerChrysler), she signed an application that contained the following provision:

> READ CAREFULLY BEFORE SIGNING. I agree that any claim or lawsuit relating to my service with Chrysler Corporation ... must be filed no more than six (6) months after the date of the employment action that is the subject of the claim or lawsuit. I waive any statute of limitations to the contrary.

The application also stated that if Thurman were hired, the application would become part of her official employment record. Thurman signed the application, acknowledging that she had read and understood it. Thurman was hired and began work at the company's Michigan facility in 1994.

In September 1999 Thurman was subjected to sexual harassment by a co-worker. She promptly complained to the company, she filed a discrimination claim with the Michigan Department of Civil Rights, and she filed a criminal complaint against the co-worker. In late February 2000, after being assigned to a different shift, she went on an indefinite leave of absence.

The co-worker was convicted of sexual assault, and he also was disciplined by Chrysler. Thurman nevertheless filed suit against Chrysler on June 1, 2000. The suit was dismissed for failure to comply with certain procedural requirements, but the court gave her permission to reinstate the suit within 30 days. Instead of reinstating, Thurman filed a second suit against Chrysler in August 2001. Chrysler asked the court to dismiss this second suit on the ground that it was filed outside the six-month period specified in Thurman's employment application.

The Sixth Circuit agreed with Chrysler that the suit was untimely. Giving Thurman the benefit of the doubt, it concluded that the six-month period began running in February 2000, when she went on leave. The initial, June 1 lawsuit was therefore filed on time. The second suit, however, filed in August 2001 was not.

In answer to Thurman's objections that the abbreviated limitations clause contained in the application was unconscionable, the Court (applying Michigan law) stated that the clause was both reasonable and prominently displayed. And in answer to Thurman's objection that six months was insufficient time to investigate her claim and prepare her suit, the Court pointed out that Thurman had already filed a lawsuit within the six-month period, presumably after adequate investigation.

References: *Thurman v. DaimlerChrysler, Inc.*, 397 F.3d 352 (6th Cir. 2004).

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OPPENHEIMER, FLEISCHER & QUIGGLE, P.C.
7700 Old Georgetown Road, Suite 800
Bethesda, MD 20814