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OPPENHEIMER, FLEISCHER & QUIGGLE, P.C. BY CHARLES H. FLEISCHER, ESQ.

Sex Discrimination and the Jealous Spouse

Title VII of the federal Civil Rights Act prohibits discrimination because of sex (among other things). But Title VII goes beyond merely prohibiting employers from preferring one gender over the other in matters of hiring, pay, promotions, job assignments, etc. It also prohibits so-called "quid pro quo" harassment – where an employee's submission to or rejection of a supervisor's sexual advances is used as a basis for employment decisions – and "hostile work environment" harassment – where an employee is subjected to severe and pervasive intimidation, ridicule or insult based on his or her gender.

But what about the employee who has a consensual relationship with his or her supervisor and, as a result, gets special treatment such as promotions or raises? Do fellow employees who are not getting the special treatment have a claim of sex discrimination? Or what if the supervisor, at the insistence of a jealous spouse, terminates the relationship and fires the employee? Is that sex discrimination?

A recent decision by the U.S. Court of Appeals for the Eighth Circuit (headquartered in St. Louis) addresses these questions.

Maelynn Tenge worked for Phillips Modern AG Co., an Iowa company, for a number of years, rising from secretary to highest-paid employee. She worked closely with the owner of the company, Scott Phillips. Scott's wife, Lori, was also involved with the company.

Scott was entirely happy with Maelynn's work, but Lori suspected that Maelynn was attempting to seduce Scott. Lori's suspicions were not without basis. For example, on two occasions, while in Lori's presence, Maelynn pinched Scott on the buttocks "for fun." Maelynn also sent a number of notes to Scott of a sexual or intimate nature.

When Lori found one of Maelynn's notes, she insisted that Scott fire Maelynn. Scott acquiesced, telling Maelynn that he was being forced to choose between his best employee and his wife and kids. This prompted Maelynn to sue, claiming sex discrimination in violation of federal and Iowa law.

The federal trial court and the appeals court both rejected Maelynn's claim. The appellate court reasoned that Maelynn was not fired because of her *sex*, but because of her *sexual conduct* – conduct Maelynn admitted and which she acknowledged could have led Lori honestly to believe she was having an affair with Lori's husband.

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The court relied on several earlier decisions ruling that when an employee receives *favorable* treatment as a result of a consensual relationship with the boss, other employees do not suffer discrimination. Again, the favorable treatment is not because of the employee's sex but because of his or her conduct. See "When the Boss's Lover Get Promoted, Do Others Suffer Sex Discrimination?", Employer Alerts, Spring 2005, p. 1.

The court also relied on an Equal Employment Opportunity Commission policy statement that "an isolated instance of favoritism toward a paramour, or a spouse, or a friend, may be unfair, but it does not discriminate against women or men in violation of Title VII, since both are disadvantaged for reasons other than their genders." However, the EEOC has also said:

> Where employment opportunities or benefits are granted because of an individual's *submission* to the employer's sexual advances or requests for sexual favors, the employer may be held liable for unlawful sex discrimination against other persons who were qualified for but denied that employment opportunity or benefit.

In other words, according to the EEOC if the relationship is consensual, then favoritism toward a paramour is permitted, but if the relationship is coercive, then other employees who do not enjoy special treatment may have a discrimination claim.

In its decision against Maelynn, the Eighth Circuit stressed that Maelynn admitted engaging in suggestive conduct which could reasonably have fed Lori's suspicions. The court made clear it was *not* deciding whether Maelynn would have had a claim had there been no suggestive conduct but had Lori nevertheless prevailed on Scott to fire Maelynn based on *un*reasonable suspicions.

References: Title VII, 42 U.S.C. § 2000e; 29 C.F.R. § 1604.11(g); *EEOC Policy Guidance on Employer Liability Under Title VII for Sexual Favoritism*, EEOC Notice No. 915-048 (Feb. 15, 1990); *Tenge v. Phillips Modern AG Co.*, 446 F.3d 903 (8th Cir. 2006).

Employer Escapes Liability for Joke Gone Bad

Southwest Airlines has a well-appreciated reputation for playfulness. Remember the flight attendant who announced over the P.A. system: "Beer and wine are $3, mixed drinks $4, and Prozac $6"? As part of this fun-loving culture, newly hired employees who have completed an initial probationary period often find themselves the subject of a prank to commemorate the occasion. In one instance, an employee who had no travel plans was led onto an airplane, the doors were sealed, and she was flown from Albuquerque to Dallas. In another instance, an employee was dressed in a hula skirt and made to perform in front of customers.

When Marcie Fuerschbach completed her probationary period with Southwest, she knew that her colleagues at Albuquerque's Sunport airport would likely play a prank on her. But she had no idea the extent to which they would go.

On the day in question, one of Fuerschbach's supervisors called the Albuquerque police department and requested that officers come to the Southwest ticket counter. When two officers arrived, a supervisor told them of a plan to subject Fuerschbach to a mock arrest as a celebratory prank. Incredibly, once the officers received assurance that Fuerschbach would "be okay" with the prank they agreed to go along.

As Fuerschbach was working at a ticket counter crowded with customers, the two officers approached her. One of them ordered Fuerschbach to go with him to answer some questions. He escorted her to the end of the ticket counter and the other officer then informed her that while performing a background check, they discovered an outstanding arrest warrant. Fuerschbach objected that there must be some mistake, but the officers interrupted and demanded that she take off her security badges and turn them in. Fuerschbach complied and handed them to a supervisor who was standing close by.

When Fuerschbach tearfully asked if this were a joke, the officers refused to reply. Instead, they placed her hands behind her back and tightly handcuffed her, and

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they led her toward an elevator, all in front of a crowd of customers and employees. Fuerschbach continued to cry. Finally, someone jumped out and yelled congratulations to her for completing probation. The officers then removed the handcuffs and the crowd began to clap, but Fuerschbach continued to cry. Later that day Fuerschbach was found weeping in a break room and was sent home. As a result of her continuing distress, Fuerschbach consulted a psychologist and was diagnosed with post-traumatic stress disorder.

Fuerschbach sued everybody – the two officers involved, the City of Albuquerque (for whom the officers worked), Southwest, and her colleagues and supervisors who participated in the prank.

The federal trial court dismissed Fuerschbach's claims on a variety of theories, but the U.S. Court of Appeals disagreed in part and sent some of the claims back for trial. The appellate court ruled that the officers' actions amounted to an arrest, since Fuerschbach could reasonably have believed she was not free to leave. (This conclusion seems rather obvious, since with handcuffs on it would have been close to impossible for Fuerschbach to walk away and return to her work.) Lacking an arrest warrant or probable cause, the officers therefore violated Fuerschbach's Fourth Amendment rights, which prohibits unreasonable searches and seizures. Furthermore, said the court, there is no "prank" exception to the Fourth Amendment.

In ruling that the officers could be liable, the court also ruled that their employer, the City of Albuquerque, could be sued as well.

However, as to Southwest and its employees, the appellate court agreed with the lower court that the New Mexico Workers' Compensation Act was Fuerschbach's exclusive remedy. In other words, Fuerschbach was limited to filing a Compensation Act claim and she could not sue Southwest or its employees for damages. In general, observed the court, in order to be covered by the Compensation Act an injury must arise out of employment. But while being falsely arrested is not normally thought of as incident to employment as an airline ticket agent, horseplay is part of many work environments.

In answer to Fuerschbach's argument that the Workers' Compensation Act does not cover intentional injuries, the appellate court ruled that none of the participants intended to injure her. Although they grossly miscalculated Fuerschbach's reaction, they all expected her to be amused by the mock arrest.

Despite Southwest's victory on appeal, one can reasonably expect a memo from corporate soon followed, directing employees to tone down their playfulness. Perhaps that is why Prozac is no longer part of Southwest's in-flight cocktail menu.

Reference: *Fuerschbach v. Southwest Airlines Co.*, 439 F.3d 1197 (10th Cir. 2006).

New Wage and Hour Rulings

The federal Fair Labor Standards Act (FLSA) requires employers to pay time and a half to non-exempt employees for time worked in excess of 40 hours per week. Three recent rulings interpret the Act's overtime provisions.

Work Requirements for Exempt Employees

In general, employees are exempt from the FLSA's overtime provisions if they are paid on a salary basis of at least $455 per week and their primary duties are executive, administrative or professional. (The FLSA and U.S. Department of Labor regulations provide for other exemptions as well.) However, employees can lose their exempt status if they are treated as hourly workers. This would happen, for example, if an employer docks the salary of an exempt employee for a personal absence of less than one day. See "Do Vacation Policies Jeopardize Exempt Status?," Employer Alerts, Summer 2005, p. 1; "Exempt Employees and Weather-Related Absences," Employer Alerts, Winter 2006, p. 2.

Under new regulations effective August 2004, DOL permits employers to discipline exempt employees for infractions of workplace conduct rules by suspending them without pay for one or more full days. As an example, the regulations cite an employer sexual harassment policy as a workplace conduct rule, violations of which qualify for suspensions.

DOL was recently asked whether an employer may adopt policies requiring exempt employees to work in excess of 40 hours per week and requiring them to make up lost time due to personal absences of less than a day. DOL ruled that such policies do not jeopardize the employees' exempt status. DOL reasoned that the number of hours worked by an exempt employee is a matter between the employer and the employee and is not subject to FLSA regulation. DOL stressed, however, that the employer may not dock an employee's pay for failure to comply with these policies. Nor may an employer treat non-compliance as a violation of a workplace conduct rule and impose a disciplinary suspension.

Docking Pay for Equipment Damage

In another recent ruling, DOL said that an employer may not fine its exempt employees, or make them pay reimbursement, for damage to or loss of company equipment, such as cell phones or laptops. This, said DOL, would violate the "salary basis" requirement for exemption, which requires that the employee be paid "a predetermined amount not subject to reduction because of variations in the quality or quantity of the work performed."

A point not mentioned in the DOL ruling is that so long as an employer pays a predetermined amount of at least $455 per week which does not vary based on quality or quantity of work, the employer may also pay additional amounts which *do* vary based on quantity or quality of work. In one case, for example, the owner of a restaurant chain paid its managers a fixed salary, plus a bonus of 2% of gross sales, but the owner deducted recurrent cash register shortages from this bonus. While that practice was permissible, when the owner switched to deducting shortages from the managers' base salaries, the managers were deemed to be hourly, non-exempt employees.

Working More Than Eight Hours Per Day

Esther Fernandez, a non-exempt employee, sued her employer, Centerplate/NSBE, Inc., under the Fair Labor Standards Act for overtime compensation. She claimed she was owed overtime for hours worked in excess of 40 hours *per week* and in excess of eight hours *per day*.

The employer produced undisputed evidence that it has paid her for all time she worked in excess of 40 hours per week. This left only the issue of overtime compensation for hours exceeding eight per day. The U.S. Court of Appeals for the District of Columbia Circuit observed that the FLSA measures overtime on a weekly, not a daily, basis. It therefore dismissed her claim.

The case illustrates an important point that employers sometimes miss in computing overtime. Suppose an employer pays every two weeks and in a given two-

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week period a non-exempt employee reports exactly 80 hours – 42 hours during week #1 and 38 hours during week #2. The employer would be incorrect in assuming that the employee is not owed overtime because he averaged 40 hours per week. Since the FLSA measures overtime on a weekly basis, two hours of overtime are due for week #1. (For these purposes, a "week" is a fixed, 168-hour period. The employer may determine when the week begins and ends, such as from Monday at 12:01 a.m. to Sunday at midnight, but the employer may not keep changing its workweek in an effort to avoid overtime obligations.)

On the other hand, suppose the employee worked ten hours on Monday of week #1. If the employee works only six hours the next day and eight hours per day for the remainder of week #1, there is no overtime obligation. In other words, compensatory time taken within the same week may be used to offset an overtime obligation, but compensatory time taken in a subsequent week may not.

References: *Fair Labor Standards Act*, 29 U.S.C. § 201; 29 C.F.R. Part 500; DOL Admin. Op. Ltr. No. FLSA 2006-6 (March 10, 2006); *DOL Admin. Op. Ltr.* No. FLSA 2006-7 (March 10, 2006); *Moore v. Hannon Food Service, Inc.*, 317 F.3d 489 (5th Cir. 2003); *Fernandez v. Centerplace/NBSE*, 441 F.3d 1006 (D.C.Cir. 2006).

Contract Ambiguity Gets Employee a Trial

In January 2002 Robert Baum, age 59, met with the president of Helget Gas Products (HGP) to discuss possible employment as an HGP salesman. Baum was then employed by a competitor and in his discussions he said he needed at least a three-year contract before he would leave the security of his current position. They also discussed starting salary, benefits, job duties, and salary increases in years two and three. Baum took detailed notes during the meeting reflecting the salary projections over the three-year period as the parties had discussed.

After further negotiations, HGP hired Baum in February 2002. Baum reminded the president of his requirement for a three-year contract, and the president promised to have Baum's meeting notes typed up and signed. After further delay, Baum asked his branch manager to sign the meeting notes. The manager (who had authority to sign for HGP) agreed and did in fact sign the notes after writing the word "Contract" on the top. Baum and the manager also added a signature line for HGP's president, but the president never signed the paper.

After some nine months of employment, HGP concluded that Baum was not meeting sales expectations, and it fired him. Baum then sued in Missouri federal court for breach of contract.

Missouri, like most states, follows the employment-at-will doctrine: In the absence of a contract that specifies the duration of employment or limits the basis on which an employee may be discharged, either party to the employment arrangement may terminate the arrangement at any time for any reason or for no reason (except, of course, an illegal reasons such as discrimination). So the question here was whether Baum's notes, which had been labeled "Contract" and which had been signed on behalf of HGP, amounted to a contract for a three-year term. Baum obviously claimed that it did, or at least that the document was ambiguous and that he should be able to present evidence of its meaning at trial. HGP said the notes did not amount to a contract, arguing that the three-year salary projections were just that – projections, not promises.

Under general contract law principles, if a contract is clear an unambiguous, then a court interpreting the contract is restricted to the "four corners" of the contract and may look no further than the words of the contract itself in determining what the contract means. On the other hand, if the words are reasonably susceptible to more than one meaning, then the parties may offer other evidence extrinsic to the contract to explain what the contract was intended to mean.

Here the court concluded that the contract was ambiguous and that Baum was entitled to a trial on the intended meaning of the contract.

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The case offers an important lesson for employers. Since most employers will want to preserve an at-will relationship and not be bound by an employment agreement, they need to choose their words carefully. When drafting an offer letter, for example, the employer should not promise, or even imply, that the job will last for a specified period of time, or that the employee can only be discharged under specified circumstances. In addition, it is good practice to say explicitly in the offer letter that the employment is at-will, and that either party can terminate the relationship at any time with or without cause.

These same considerations apply to employee handbooks, which the courts have sometimes held amount to contracts of employment. An employer who wishes to adopt an employee handbook but who does not want to be contractually bound by its provisions can take steps to reduce, if not eliminate, the risk of contractual liability by –

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

Reference: *Baum v. Helget Gas Products, Inc*, 440 F.3d 1019 (8th Cir. 2006).

Pregnant Employee Not Entitled to Light Duty

Swift Transportation, a Tennessee trucking company, had an established policy of offering light duty only to employees who were on workers' compensation leave – that is, employees who had sustained on-the-job injuries. Employees who were subject to work restrictions due to medical conditions other than on-the-job injuries were not offered light duty and were subject to termination if unable to perform their regular responsibilities.

When Amanda Reeves went to work at Swift, she was told that her job as a truck driver required occasional bending, twisting, climbing, squatting, crouching and balancing. In addition, she might have to use a dolly to push freight weighing up to 200 pounds and to push freight of up to 100 pounds using brute force. Reeves signed a form saying she was capable of such physical activity and that she could lift 75 pounds and carry it 56 feet and could lift 60 pounds over her head.

After three months on the job, Reeves learned she was pregnant. Her obstetrician restricted her to light duty and told her not to lift more than 20 pounds. Reeves informed Swift of these restrictions and asked for light duty. Swift responded that, consistent with its established policy, it had no light duty for her.

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In contrast, Swift had assigned light duty, such as office work, answering phones, entering orders and filing, to employees who had sustained work-related injuries. Having no work for Reeves, Swift fired her. She then sued, claiming discriminatory treatment because of sex under Title VII of the federal Civil Rights Act. (As amended by the Pregnancy Discrimination Act, Title VII defines sex discrimination to include discrimination because of pregnancy, childbirth, or related medical conditions.)

The U.S. Court of Appeals for the Sixth Circuit rejected Reeves's claim. It said that Swift's light-duty policy was "pregnancy-blind" since it neither granted nor withheld light duty assignments on the basis of pregnancy. Instead, the policy used a non-discriminatory criterion of whether the employee's medical restriction arose from work-related or non-work-related causes.

The Court twice pointed out in its written opinion that Reeves brought her suit under a theory of *disparate treatment*, that is, that she had been treated differently from other employees because she was pregnant. But in addition to disparate treatment, Title VII also prohibits employer policies that, while non-discriminatory on their face, have an unintended, adverse impact on minorities, women, and other protected groups.

These are known as *disparate impact* claims. The classic example is an employer who imposes minimum height and weight requirements which have no business justification but which favor men candidates over women candidates.

By stressing that Reeves's suit relied only on a disparate treatment theory, the Sixth Circuit implied that had she included a disparate impact claim she might have fared better. After reading the Sixth Circuit's opinion, Reeves's attorney likely contacted his malpractice insurance carrier.

References: Title VII, 42 U.S.C. § 2000e; *Reeves v. Swift Transp. Co.*, 446 F.3d 637 (6th Cir. 2006); *Raytheon Co. v. Hernandez*, 124 S.Ct. 51303).

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In this issue of EMPLOYER*ALERTS* . . .

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

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OPPENHEIMER, FLEISCHER & QUIGGLE, P.C. BY CHARLES H. FLEISCHER, ESQ.

Don't Tell Me You Have Jury Duty

It always seems to happen at crunch time. You're in the midst of preparing a major contract proposal, the deadline is just a few short weeks away, and the team leader announces she's been summoned for jury duty. How do you respond? And is there anything you can legally do to reduce the hardship?

The courts generally notify potential jurors well in advance of the date they are likely to be called. So if you are hearing about a jury summons at the last minute, it's probably because your employee failed to let you know sooner. This should be addressed by a provision in your employee handbook along the following lines:

> Employees must notify their supervisors as soon as possible of anticipated absences, such as for jury duty, military service, etc. The Company may require the affected employee to document the absence by providing a copy of the jury summons or military orders.

Even with advance notice, the team leader's absence may substantially disrupt the project. Most courts recognize this and are receptive to a one-time, reasonable request for postponement. If the jury summons comes at a particularly inconvenient time, the employer, the employee, or both, should write to the court official who issued the summons, explain the problem, and ask for a short delay. The letter should give a date when the workplace crunch is expected to be over and the affected employee will be available for service. The letter should also be supported by relevant documentation. For example, if the affected employee is scheduled to attend an out-of-town meeting at the time of jury service, attach a copy of her travel itinerary and explain in the letter why the meeting is important to the company.

Most important, be truthful in requesting a postponement. Suggesting that the employee "Do whatever it takes to get out of jury service ... tell them you moved out of state" could subject both you and your employee to criminal charges, including perjury.

Taking adverse action against the employee herself is also prohibited. Federal law protects the jobs of employees who are called as jurors in U.S. District Court. Remedies for violation of this provision include reinstatement of the employee, payment of back wages, a civil fine of up to $1,000 for each violation, and payment of the employee's attorney fees. Most states (including Maryland, the District of Columbia and Virginia) also provide job protection for employees who are summoned to serve in state courts.

Some courts have held that an employer has an affirmative duty to let its employees know they will not suffer any reprisal for reporting to jury duty as summoned. An employee manual provision such as the following is recommended:

> The Company encourages employees to fulfill their civic obligation to serve as jurors when summoned. The Company will not discharge, threaten to discharge, intimidate, or coerce any employee by reason of such employee's jury service, or the attendance or scheduled attendance in connection with such service.

In a recent case, Judge Alexander Williams of the U.S. District Court for Maryland allowed a suit brought by a terminated employee of ACS Government Services to go forward. The employee, Richard Shaffer, claimed that he had been fired when he was ordered to report for grand jury service for two days each week over a period of months. (Grand juries sit for up to 18 months on

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a sporadic basis to consider whether criminal suspects should be indicted. Petit juries hear civil and criminal trials.) The employer claimed that the firing was for unsatisfactory job performance. Judge Williams found that the employer's explanation was not believable, in part because the employer failed to preserve a draft version of a memo by the employee's former supervisor regarding the termination.

Back to the team leader on your contract proposal. With crunch time over and the proposal submitted, the day finally comes for her to report for jury service. On her way out the door she asks, "Will you be paying me my usual salary while I'm on jury duty? And will I lose annual leave while I'm away?"

In Maryland there's no obligation to pay an employee during absences for jury service, but employers are prohibited from charging the absence against leave.

Full-time employees in the District of Columbia are entitled to their usual compensation less fees received for jury service of five days or less. (It is unclear whether, if jury services extends to more than five days, the employer need not pay at all. The safest practice would be to pay the first five days even if her service extends longer than that.) District law is also silent on whether absence for jury service may be charged against leave, but since charging the absence against leave could be viewed as an adverse action, the safest practice would be not to reduce annual leave for time spent on jury duty.

Virginia is similar to Maryland: there is no requirement that an employer pay its employees while they are on jury service, but the employer cannot charge absences against leave.

Even when the law does not require jurors to be paid while serving, employers should consider the effect of not doing so on an exempt employee's status. Exempt employees are not entitled to time and a half for overtime – time worked in excess of 40 hours per week. But if exempt employees are treated like hourly workers, they loose their exempt status and become entitled to overtime. See "Do Vacation Policies Jeopardize Exempt Status?" Employer Alerts, Summer 2005, p.1.

U.S. Department of Labor regulations provide that if an exempt employee who is absent for jury service works any part of a week, he is entitled to full pay for that week (less any fees he receives for jury service). Thus docking the pay of an exempt employee who is on jury duty for part of a week and who works the remainder of the week jeopardizes the employee's exempt status.

References: 28 U.S.C. §1875; Md. Code, C&JP § 8-501; D.C. Code § 15-718; Va. Code § 18.2-465.1; *Jones v. Marriott Corp.*, 609 F.Supp. 577 (D.D.C.1985); *Shaffer v. ASC Govt. Svcs., Inc.*, 2006 WL 2788241 (2006); 29 C.F.R. § 541.602(b)(3).

Accommodating Religious Observance and Practice

Title VII of the federal Civil Rights Act makes it illegal for an employer to discriminate against an employee on the basis of his or her religion. This means, for example, that an employer cannot refuse to hire an applicant because the applicant is a member of a particular religious sect, any more than the employer can refuse to hire an applicant on the basis of the applicant's race or gender. Harassment based on religion is also a violation of Title VII.

But religion gets additional special treatment under Title VII. Title VII defines "religion" to include all aspects of religious observance and practice, as well as belief, unless an employer demonstrates that he is unable to reasonably accommodate an employee's or prospective employee's religious observance or practice without undue hardship on the employer's business. See "Dress Code Trumps Duty of Religious Accommodation," Employer Alerts, Winter 2005, p. 4, in which an employee unsuccessfully claimed that as a member of the Church of Body Modification, she should be allowed to pierce various visible body parts in violation of her employer's dress code.

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A recent case from New Jersey provides a good illustration of this principle.

Stuart Aron, an orthodox Jew, applied for a job as a phlebotomist with Quest Diagnostics. Quest provides clinical testing services for hospitals, government agencies, and other health care providers. Quest requires each of its employees to work two Saturdays per month and, when it learned that Aron would not work on Saturdays for religious reasons, it refused to hire him.

In Aron's subsequent lawsuit, Quest showed that it adopted the Saturday work requirement several years earlier in response to demands for increased weekend services. Quest also showed that it enforced this requirement for all employees and that granting any exceptions would result in unequal treatment and a lowering of employee morale.

Although Aron contended that Quest could, with minimal cost, accommodate him by hiring other phlebotomists to cover his Saturday obligation, Aron failed to support that with any evidence.

The court agreed with Quest that accommodating Aron's religious observance and practice would be unreasonable. The court therefore dismissed Aron's suit.

References: 42 U.S.C. § 2000e; *Aron v. Quest Diagnostics Inc.*, 2006 WL 859034 (3rd Cir. 2006).

Taxation of Settlement Proceeds in Employment Cases

The taxation of settlement proceeds in employee lawsuits for discrimination, wrongful discharge, unpaid overtime, etc., continues to be confusing both for employers and for their attorneys and accountants as well. The main issues are whether the proceeds are taxable at all; if so, whether they should be treated as wages for income tax withholding and payroll tax purposes; and when the payment is made by a third party, such as the employer's insurance company, whether the employer or the third party has IRS reporting obligations. The issues become even more complicated when a portion of the settlement proceeds is allocated as fees to the employee's attorney.

Failure to comply with applicable rules can subject the employer to penalties and the employer's management to personal liability.

Income Taxation

First some basic rules. The Internal Revenue Code generally taxes all "gross income," which is defined as "all income from whatever source derived," including compensation for services, fees, commissions, fringe benefits, and similar items. Any accession to wealth received in settlement of a lawsuit falls within the definition of "gross income" and is subject to income taxation unless some other statutory provision excludes the settlement proceeds from gross income.

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Suppose an employee is fired after complaining about sexual harassment. She then brings suit for the harassment and for the retaliatory firing. Later the parties reach a settlement which provides for payment of $100,000 to the employee. In their settlement agreement, the parties attribute $50,000 to wages the employee lost between the firing and the settlement, and they attribute $50,000 to emotional distress caused by the harassment and illegal firing.

Clearly the $50,000 attributable to lost wages will be gross income subject to taxation. But what about the $50,000 attributable to emotional distress? Since the payment is not excludible as a payment for "personal physical injuries," it therefore constitutes gross income as well. At least according to the IRS.

In determining whether a particular settlement payment falls within the definition of gross income, the IRS and the courts look at the origin and nature of the claim that underlies the lawsuit. For example, in a suit for unpaid overtime, the origin and nature of the claim relates to wages, even though the employee might try to characterize the claim as something else. Therefore, a settlement of the suit will result in taxable income.

Although certain payments might appear to fall within the definition of gross income, the Internal Revenue Code provides for a variety of exclusions from gross income. One of these exclusions is for damages received on account of personal physical injuries or physical sickness. The victim of a car accident for example, who recovers damages for his pain and suffering, may exclude the damages from gross income.

The Code provision goes on to say that *emotional distress* shall *not* be treated as a physical injury or physical sickness. In a private letter ruling the IRS has also defined the term "personal physical injuries" as "direct unwanted or uninvited physical contacts resulting in observable bodily harms such as bruises, cuts, swelling, and bleeding." In other words, under the Code, a person who suffers emotional distress without any accompanying physical injury cannot take advantage of the "personal physical injuries" exclusion and must include any settlement payments in gross income.

But the IRS may not have the last word on this issue. In the recent case of *Murphy v. IRS*, the U.S. Court of Appeals for the District of Columbia Circuit ruled that the Internal Revenue Code's definition of "gross income" is unconstitutional to the extent it purports to tax payments for emotional distress. The Court reasoned that prior to adoption of the Sixteenth Amendment to the Constitution, Congress had no power to impose an income tax. With adoption of that Amendment in 1913, Congress was granted the power to tax income, but it still could not tax mere restoration of capital. (For example, if you buy $1,000 worth of corporate stock and sometime later you sell it for exactly $1,000, you have simply realized a restoration or your capital; you have not received income.) Following this reasoning, the Court ruled that the proceeds of a personal injury suit – whether for physical *or* emotional injury – are a return of (human) capital and not income.

The *Murphy* decision is not likely to be the last word either. Stay tuned.

Employment Taxes

Assuming that a particular settlement payment falls within the definition of gross income and that it is not subject to any exclusion, the next issue is whether the payment is subject to withholding of income tax and to payment of social security tax (FICA) and federal unemployment tax (FUTA). This in turn depends on whether the payment

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constitutes "wages," which the Internal Revenue Code broadly defines as "all remuneration for services performed by an employee for his employer."

The "origin of the claim" concept also applies here. Suppose a high-level executive has a three-year contract with his company at an annual salary of $175,000. After two years the company is dissatisfied with the executive's work and fires him. The executive then sues for breach of contract, claiming the $175,000 he would have earned during the last year of the contract. The parties eventually settle for $100,000. The payment will be treated as wages paid to the employee for employment and subject to withholding, FICA and FUTA.

For the same reason, a signing bonus will also be treated as wages.

Returning to the example in which the parties allocated $50,000 to lost wages and $50,000 to emotional distress, clearly the first $50,000 is wages subject to income tax withholding and to FICA and FUTA. While the $50,000 balance would seem not to be wages, the question is whether the IRS will respect the parties' allocation. (The fact the payment is made after the employment relationship has ended doesn't matter in determining whether the payment constitutes wages.)

The IRS says it is not necessarily bound by the parties' allocation and it will disregard the allocation where the facts and circumstances indicate that the allocation does not reflect the economic substance of the settlement. In a Technical Advice Memorandum issued in 2002, the IRS considered settlement agreements in two employment discrimination cases. In one case the parties allocated one-half to lost wages and one-half to emotional distress. In the other case they allocated only one-third to wages and the remaining two-thirds to emotional distress. The IRS accepted the 50% allocation, but it rejected the allocation of two-thirds to emotional distress.

Attorney Fees

To complicate matters further, suppose the settlement agreement provides that of the $100,000 payment, $33,333 is payable directly to the employee's attorney and the balance is payable to the employee. Prior to 2004, the IRS and most courts took the view that the entire $100,000 was taxable to the employee, although the employee could then take a miscellaneous deduction for the attorney fee payment. (Remember, however, that a miscellaneous deduction is available only to a taxpayer who itemizes and the amount of the deduction is subject to limitations.)

The American Jobs Creation Act of 2004 addressed this situation by excluding from gross income the fees and costs paid in connection with unlawful workplace discrimination claims. 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. A final catchall provision allows exclusion of attorney fees in connection with suits under any Federal, State, or local statutory or common law providing for the enforcement of civil rights, or regulating any aspect of the employment relationship.

Withholding and Reporting Responsibility

Using the example of a $100,000 settlement, of which $33,333 is allocable to lost wages payable to the employee, $33,333 is allocable to emotional distress payable to the employee, and $33,333 is allocable to fees payable to the attorney, the employer will have the following withholding and reporting obligations:

- *$33,333 for lost wages*: This is subject to income tax withholding and FICA and FUTA. The payment is reportable on Form W-2.

- *$33,333 for emotional distress*: This is taxable income (unless the Court's decision in *Murphy v. IRS* is upheld, in which case it is unconstitutional to tax emotional distress awards). However, assuming the allocation is reasonable, this is *not* subject to income tax withholding or to FICA and FUTA. The payment is reportable on Form 1099-MISC.

- $33,333 for attorney fees: This is also taxable income. However, it is *not* subject to income tax withholding or to FICA and FUTA. The payment is reportable on *two* 1099-MISC forms, one issued to the employee and the other issued to the attorney.

(continued)

In summary, the employee will get a W-2 for $33,333 and a 1099-MISC for $66,667 and he may deduct $33,333 as an adjustment to gross income. The attorney will get a 1099-MISC for $33,333.

As to the portion subject to W-2 withholding and reporting, the employer should use withholding rates in effect at the time of the settlement payment, even though the payment relates to wages that became due at some earlier time, when different rates may have been in effect.

Third Party Payments

Sometimes the actual settlement payments will be made not by the employer but by a third party. For example, the employer may have an indemnity arrangement in place requiring someone else to make the payments. More likely, the employer will have obtained employment practices liability insurance coverage and the insurance company will be making the payments.

In such cases, the third party stands in the employer's shoes and may be responsible for the same reporting obligations that the employer would have faced had the employer made the payments. IRS regulations provide that a person who makes a payment in the course of its trade or business on behalf of another person must make a return of information if the payor either performs management or oversight functions in connection with the payment, or has a significant economic interest in the payment. Where an insurance company is authorized to settle claims and it makes settlement payments in discharge of its policy obligations, the insurance company will likely have the duty of reporting the payments to the IRS.

References: IRC §§ 61, 62, 104; IRS Regs. 1.6041-1(e); Rev. Rul. 2004-109; Rev. Rul. 2004-110; TAM 200244004 (2002); PLR 200041022 (2000); *Appoloni v. U.S.*, 450 F.3d 185 (6th Cir. 2006); *Ward v. American Family Life Ins. Co.*, 444 F.Supp.2d 540 (D.S.C. 2006); *Murphy v. IRS*, 460 F.3d 79 (D.C. Cir. 2006); *U.S. v. Cleveland Indians Baseball Co.*, 532 U.S. 200 (2001).

Paying Wages in Foreign Currency

To qualify as exempt from overtime under one of the so-called "white collar" exemptions, an employee must not only satisfy the *duties* test (that is, his or her duties must meet the definition of executive, administrator, or professional), but in most cases the employee must satisfy the *salary basis* test as well. Under the salary basis test, an employee must in general be paid a salary of $455 per week ($23,660 per year). What if your employee is a foreign national who is paid partly in U.S. currency and partly in the currency of his home country? Will the foreign currency component count in satisfying the salary basis test?

The U.S. Department of Labor recently ruled on the question. It concluded that if the U.S. component and the foreign component, converted to U.S. dollars using the prevailing exchange rate, together equal or exceed the $455 threshold, then the employee qualifies as exempt.

Although counting a foreign currency component may satisfy the Department of Labor, employers should be aware that all three local jurisdictions – Maryland, Virginia and the District – require wages to be paid in U.S. currency or by check that can be cashed at face value for U.S. currency. In both Maryland and Virginia, payments may also be made by direct deposit or by crediting a debit card, but only if the employee agrees. District law is silent on the subject of direct deposits and debit card payments.

References: 29 U.S.C. § 201; 29 C.F.R. Part 541; DOL Opinion FLSA 2006-17 (May 23, 2006); Md. Code, L&E § 3-502(c)(1); Va. Code § 40.1-29(B); D.C. Code § 32-1002(8).

Charge Nurses Are Supervisors for Labor Law Purposes

The National Labor Relations Act (NLRA) gives employees the right to form unions. It also requires employers to bargain with union representatives in good faith over matters that are directly germane to the workplace, such as wages, hours, and working conditions. However, supervisory employees generally have no rights under the NLRA, since they may not be included in bargaining units and employers have no duty to bargain with them.

For federal labor law purposes, a "supervisor" is a person with genuine management prerogatives who exercises independent judgment in making personnel assignments or in directing others in the performance of their duties.

Nurses and other professionals have long been allowed to organize (although as professional employees, nurses cannot be forced into a bargaining unit with non-professionals). The typical hospital setting includes not only RNs, who do hands-on patient care, but also charge nurses, who are RNs responsible for overseeing patient care units, assigning RNs and other staff to specific patients, monitoring patients, meeting with physicians and families of patients, and following up on unusual incidents.

The National Labor Relations Board recently ruled that nurses who are *permanently* assigned as charge nurses are supervisors who cannot be union members. (*Rotating* charge nurses – RNs who normally provide hands-on patient care but who occasionally are assigned as charge nurses – are not supervisors and they qualify for union membership.) This ruling could have a significant impact on compensation for permanent charge nurses. As professionals, they are exempt from the overtime pay requirements of federal law. To the extent they negotiated for overtime in their union contracts, they will no longer have the benefit of those contracts.

Reference: 29 U.S.C. § 151; *Oakwood Healthcare, Inc.*, 348 NLRB No. 37 (2006); *Beverly Enterprises-Minnesota, Inc.*, 348 NLRB No. 39 (2006); *NLRB v. Kentucky River Community Care*, 532 U.S. 706 (2001); 29 C.F.R. § 541.301(e)(2).

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In this issue of EMPLOYER*ALERTS* . . .

- **Don't Tell Me You Have Jury Duty**
- **Accommodating Religious Observance and Practice**
- **Taxation of Settlement Proceeds in Employment Cases**
- **Paying Wages in Foreign Currency**
- **Charge Nurses Are Supervisors for Labor Law Purposes**

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

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By Charles H. Fleischer, Esq.

New Regs Implement DC's Gender Identity Discrimination Law

Last March the District of Columbia Council passed legislation to add *gender identity or expression* to the list of characteristics that cannot be considered in making employment decisions. Under the statute, a D.C. employer cannot harass, refuse to hire, or otherwise discriminate against an employee who identifies with a gender opposite his or her original, biological gender.

The D.C. Human Rights Commission has now adopted regulations to implement the statutory change. Under the new regulations, an employer cannot require employees to dress or groom themselves in a manner inconsistent with their gender identity or expression. This means, for example, that if an employee who is a biological male self-identifies as a female, the employee must be permitted to dress and groom as a woman. The employee must also be granted access to gender-specific facilities consistent with the employee's gender identity or expression, so that an employee who is a biological male must be permitted to use the women's bathroom and dressing room. It makes no difference that the employee has not undergone sex-change surgery and remains a biological male.

Employers must also grant medical leave for transgender-related health care needs, such as counseling and surgery, to the same extent that leave is granted for other medical needs.

Under the new regulations, an application for employment may answer gender-related questions based on the gender that he or she identifies with, rather than his or her biological gender.

Similarly, an applicant may give a name consistent with the applicant's gender identity, rather than his or her legal name. The regulations do, however, permit an employer to insist upon the applicant's proper legal name when use of that name is required by law or when the employer has a reasonable business purpose for obtaining the information.

Should an employer learn through a background check or other means that an applicant or employee is transgender, the employer not only cannot take adverse action against the person, the employer must take reasonable efforts to preserve the confidentiality of the information.

The District's gender identity statute and regulations are too new to have been tested in court. A handful of cases from other jurisdictions may give some indication of how District law could be interpreted.

Federal

At the federal level, prior to the Supreme Court's 1989 decision in *Price Waterhouse v. Hopkins* the lower federal courts consistently ruled that Title VII's prohibition of *sex* discrimination does not cover *transgender* discrimination. (Title VII is the principal federal civil rights law prohibiting discrimination in employment.)

Price Waterhouse has led some courts to think differently. In *Price Waterhouse*, a female senior manager was denied partnership in her firm because she was considered too "macho" for a woman. She was told that her chances for partnership would improve if she took a course at charm school and she dressed and behaved in a more feminine manner. The Supreme Court held that this type of gender stereotyping amounts to sex discrimination under Title VII.

Relying on *Price Waterhouse*, some courts have reasoned that discrimination against a transgender individual is nothing more than gender stereotyping in violation of Title VII.

A March 2006 decision by Judge James Robertson of the U.S. District Court for D.C. in *Schroer v. Billington* offers a different approach to the issue. Schroer, a biological male, was diagnosed with gender dysphoria – a condition in which a person's gender identity conflicts with his or her anatomical sex. According to one authority cited in Judge Robertson's opinion, treatment typically consists of three steps: presenting oneself full-time as a gender corresponding to one's identity rather than one's anatomy (the "real life" test); hormone therapy; and, finally, sex reassignment surgery.

(It should be noted that although gender dysphoria is considered a medical condition, is does not qualify as a disability under the Americans with Disabilities Act. The ADA defines *disability* to exclude transvestism, transsexualism, pedophilia, exhibitionism, voyeurism, gender identity disorders not resulting from physical impairments, or other sexual behavior disorders.)

While still presenting as a male, Schroer applied for a research position with the Library of Congress, a position for which he was highly qualified. He was offered and accepted the position. At that point he explained to his employer that he was under a physician's care for gender dysphoria and, according to the treatment plan, would start work presenting as a woman. The next day he was informed that the job offer was withdrawn.

Judge Robertson rejected the notion that the Supreme Court's *Price Waterhouse* decision provides authority for treating transgender discrimination as a violation of Title VII. However, he went on to say that pre-*Price Waterhouse* cases may simply be wrong. That is, discrimination against a person because he or she is transgender may well be discrimination because of sex. He therefore concluded that Schroer should be allowed to develop an appropriate factual record and that Shroer's suit should not be dismissed out of hand.

The Supreme Court will likely have the final word on just what it meant in *Price Waterhouse* and whether Title VII applies to transgender discrimination.

Minnesota

After working for the Minneapolis school district for nearly 30 years, David Nielson informed the school administration that he identified with the female gender and would be transitioning to Debra Davis. On receipt of this information, and after consulting with its attorneys, the school district concluded that Nielson-Davis should be allowed to use a female restroom.

A female teacher objected, claiming that Nielson-Davis's use of the female restroom amounted to religious and sex discrimination against her. The U.S. Court of Appeals for the Eighth Circuit rejected the female teacher's claim, pointing out that by using a more distant facility – a matter of inconvenience only – she could avoid encountering Nielson-Davis in the restroom.

New York

A trial-level court in Westchester County held that New York State's law against *sex* discrimination is broad enough to cover *transgender* discrimination.

References: D.C. Code § 2-1402.11; 53 D.C. Register 8751 (Oct. 27, 2006); 42 U.S.C. § 12211; *Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989); *Ulane v. Eastern Airlines, Inc.* 742 F.2d 1081 (7th Cir. 1984); *Etsitty v. Utah Transit Auth.*, 2005 WL 1505610 (D.Utah 2005); *Kastl v. Maricopa Cnty. Comm. College*, 2006 WL 2460636 (D.Ariz. 2006); *Schroer v. Billington*, 424 F.Supp.2d 203 (D.D.C. 2006); *Cruzan v. Minneapolis Special School Dist.*, 294 F.3d 981 (8th Cir. 2002); *Buffong v. Castle on the Hudson*, 2005 WL 4658320 (N.Y.Supr. 2005).

Mailing Errors Are Costly to Employers

Hard Rock Café v. D.C. Dept. of Employment Services

The District's Workers' Compensation Act says that once benefits are awarded they must be paid within 10 days. If the benefits are not timely paid, the D.C. Department of Employment Services (DOES) must order the employer to pay a 20% penalty on top of the award, unless the employer can show that benefits could not be timely paid due to conditions outside the employer's control.

Jerome McGinnis and his employer, Hard Rock Café, entered into a settlement agreement of McGinnis's workers' comp claim which required the employer to pay a lump sum of approximately $63,000. DOES approved the settlement and sent a certification to the employer's insurance carrier, Liberty Mutual, stating that the award must be paid within 10 days. The certification contained McGinnis's current address in Falls Church, Virginia.

Liberty Mutual mailed a check to McGinnis within the 10-day time limit, but sent it to McGinnis's former address where he no longer resided. When McGinnis's attorney notified the carrier that McGinnis had not received payment, Liberty Mutual promptly stopped payment on the first check and replaced it with a second check, this time mailing it to McGinnis's Falls Church address.

Because the second check was mailed outside the 10-day time limit, McGinnis's attorney asked DOES to add a 20% penalty to the award. DOES ordered payment of the penalty, finding no basis to excuse the employer's lateness. The employer then appealed to the D.C. Court of Appeals.

The Court of Appeals noted that during the course of the workers' compensation proceeding, McGinnis's lawyer had filed papers with DOES, with copies to Hard Rock Café and Liberty Mutual, in which McGinnis's current address was shown. Thus, according to the Court, the employer was or should have been on notice of the correct address. Concluding that the 20% penalty – amounting to some $12,600 – should be upheld, the Court said:

> We do not dispute that the employer (and Liberty Mutual) acted in complete good faith in reissuing the check as soon as they learned of its non-receipt and stopped payment on the first one; and McGinnis claims no financial harm from the delayed payment even remotely commensurate with the 20% penalty imposed. But the statute as drafted makes such considerations beside the point, by penalizing – in a readily administrable percentage amount – employers who through their own fault or inattention fail to pay compensation in the timely manner required.

Crotty v. Dakotacare

The federal law known as COBRA requires covered employers (generally, all employers who sponsor group health insurance plans and have 20 or more employees) to notify employees who quit or are fired (unless fired for gross misconduct) that they have the option to continue health insurance coverage for a limited period at their own expense. In general, the notice must be given within 14 days after the plan administrator becomes aware of the termination.

Kelly Crotty worked for Big D Oil Company in South Dakota and participated in the company's group health insurance plan. The plan was administered by a separate entity known as Dakotacare Administrative Services.

Crotty was laid off when Big D closed one of its retail locations. According to Crotty, she never received notice of her COBRA continuation rights, but she did receive a later notice from Dakotacare that her time to elect continuation coverage had expired. In the interim she had developed medical problems that eventually required surgery. When Crotty received the expiration notice she attempted to elect continuation coverage but Dakotacare rejected her attempt as untimely. Crotty then sued.

The U.S. Court of Appeals for the Eighth Circuit first observed that the burden is on the plan administrator – here, Dakotacare – to prove compliance with COBRA's notice requirement. Although proof of actual receipt of notice by the former employee is not necessary, the plan administrator must at least show a good faith attempt at compliance by sending the notice in a way reasonably calculated to reach the recipient.

In this case, all Dakotacare could produce was an audit report indicating that its computerized tracking system had generated a notice letter to Crotty around the time she was terminated. A witness also described how the tracking system worked and she described the standard procedure for sorting and mailing notices. However, Dakotacare produced no evidence at all that the procedure was followed in this case. Specifically, Dakotacare failed to show that the notice letter was actually printed, placed in a properly addressed envelope, and sent through the mail.

Therefore, concluded the Court, Dakotacare did not establish that it took steps reasonably calculated to give Crotty notice of her COBRA rights. In sending the case back to the trial court for further proceedings, the Court of Appeals did not say just what remedy Crotty was entitled to. Presumably, however, someone other than Crotty will be liable for all the medical bills that should have been but were not covered by COBRA.

References: D.C. Code § 32-1501; 7 D.C.M.R. § 200; *Hard Rock Café v. D.C. Dept. of Employment Svcs.*, 2006 WL 3370175 (D.C. 2006); 29 U.S.C. § 1161; *Crotty v. Dakotacare Admin. Svcs., Inc.*, 455 F.3d 828 (8th Cir. 2006).

Recent FMLA Rulings

Under the Family and Medical Leave Act (FMLA), a *covered employer* must:

- grant an *eligible employee* up to 12 weeks per year of unpaid leave for a serious health condition, to care for a spouse, child or parent with a serious health condition, or to care for a newborn or newly adopted child;
- restore the employee to his former job upon return to work, or to an *equivalent job* (a job that is virtually identical to the former job in terms of pay, benefits, and other employment terms and conditions);
- maintain group health insurance coverage for the employee, including family coverage, on the same basis as if the employee had continued to work; and
- preserve for the employee any benefit that accrued prior to taking leave.

A *covered employer* is an employer that has 50 or more employees for at least 20 weeks during the current or preceding calendar year. An *eligible employee* is an employee who has been on the job for at least 12 months, who has worked at least 1250 hours during the previous year, and who works at a location such that at least 50 employees are employed within 75 miles of that location.

Recent cases address some of the issues that can arise under FLMA.

50-Employee Requirement

Leanne Engelhardt worked for S.P. Richards Co., an office supply wholesaler in Nashua, New Hampshire. Richards employed fewer than 50 people. Richards was a wholly-owned subsidiary of Genuine Parts Co. (an auto parts retailer doing business as NAPA Auto Parts), whose employees, when added to those of Richards, totaled at least 50.

Engelhardt was fired after missing work to care for her daughter. It was Engelhardt's third unauthorized absence for the same reason. Claiming FMLA protection, Engelhardt sued.

Faced with the fact that Richards itself employed fewer than 50 employees, Engelhardt argued that the subsidiary and parent companies should be considered "integrated" (i.e., a single employer), based on Richard's having adopted many of Genuine Parts's human resources policies. To support her argument she cited DOL regulations which allow for treatment of separate employers as integrated or single employers according to the following factors:

- common management;
- interrelation between operations;
- centralized control of labor relations; and
- degree of common ownership/financial control.

Applying these factors, the Court concluded that Richards and Genuine Parts were *not* integrated companies. For example, they were in separate lines of business, they had separate worksites and separate management, and they maintained separate human resources departments. The fact that Richards had adopted many of Genuine Parts's policies did not mean it was required to do so or that it wasn't free to adopt different policies if it wished.

12-Months On-the-Job Requirement

Kenneth Rucker worked as a car salesman for Lee Auto Malls in Maine for five years. He left that position and, five years later, rejoined Lee Auto Malls. Seven months after that he took medical leave for a ruptured disc. Lee Auto Malls then fired Rucker and Rucker sued, claiming his leave was protected under FLMA.

The issue before the U.S. Court of Appeals for the First Circuit was whether Rucker's two periods of employment should be considered together in determining the 12-month on-the-job requirement; or, alternatively, whether a break in service starts the 12-month clock running anew.

The Court found the COBRA statute itself ambiguous on the issue, so it looked to regulations of the U.S. Department of Labor. Those regulations say:

> The 12 months an employee must have been employed by the employer need not be consecutive months. If an employee is maintained on the payroll for any part of a week, including any periods of paid or unpaid leave (sick, vacation) during which other benefits or compensation are provided by the employer (e.g., workers' compensation, group health plan benefits, etc.), the week counts as a week of employment. For purposes of determining whether intermittent/occasional/ casual employment qualifies as "at least 12 months," 52 weeks is deemed to be equal to 12 months.

The Court concluded that DOL's regulations were ambiguous as well: while the first sentence flatly says that the 12 months need not be consecutive, the following sentences seem to imply that the employee must at least maintain some relationship with the employer during a break in service, such as being carried on the employer's payroll.

The deciding factor was that the DOL has consistently interpreted its own regulations as *not* requiring consecutive service. Therefore, Rucker's break in service did not disqualify him from eligibility for FMLA leave.

75-Mile Requirement

A recent case addresses whether the 75-mile requirement refers to "linear" miles (i.e., "as the crow flies"), or "surface" miles (i.e., the distance one would actually have to travel using existing roads or other available forms of transportation).

Kelly Hackworth worked for Progressive Casualty Insurance Company in Norman, Oklahoma. Progressive had 47 employees at its Norman worksite, plus an additional three in Lawton, Oklahoma. According to the evidence presented, Norman and Lawton are 67 linear miles apart but are separated by 75.6 surface miles.

The U.S. Court of Appeals for the Tenth Circuit held that Hackworth did not qualify for FMLA benefits because the 75-mile requirement is determined using surface, not linear, miles. The Court relied on DOL regulations that state:

> The 75-mile distance is measured by surface miles, using surface transportation over public streets, roads, highways and waterways, by the shortest route from the facility where the eligible employee needing leave is employed. Absent available surface transportation between worksites, the distance is measured by using the most frequently utilized mode of transportation (e.g., airline miles).

Preservation of Accrued Benefits

Robert Sommer took eight weeks of FMLA leave from his employment at the Vanguard Group in Pennsylvania. As a Vanguard employee, he was entitled to participate in the company's bonus plan, which determined individual bonuses based on job level, length of service, and hours worked. Under the plan, "hours worked" included paid leave of absence, such as vacation and sick leave, but excluded unpaid leave, such as FMLA leave. The plan provided that if an employee's "hours worked" were fewer than 1950 hours per year, the bonus to which he would otherwise be entitled would be reduced on a pro rata basis.

When Sommer's bonus was reduced on account of his FMLA leave, he sued, claiming that Vanguard was interfering with the exercise of his rights under FMLA.

Again, DOL regulations and rulings played a decisive role in resolving Sommer's claim. DOL distinguishes, for example, between bonuses for perfect attendance (which cannot be withheld because an employee took FMLA leave) and performance-based bonuses based on production goals or hours worked (which may be prorated based on FMLA leave). Based on these regulations and rulings the Court upheld Vanguard's bonus plan and agreed that Sommer's bonus payment could be prorated.

References: 29 U.S.C.§ 2601; 29 C.F.R. § 825.101; *Engelhardt v. S.P. Richards Co.*, 2006 WL 3759330 (1st Cir. 2006); *Rucker v. Lee Holding Co.*, 2006 WL 3704457 (1st Cir. 2006); *Hackworth v. Progressive Ins. Co.*, 468 F.3d 722 (10th Cir. 2006); *Sommer v. Vanguard Group*, 461 F.3d 397 (3d Cir. 2006); DOL Opinion Ltrs. FMLA-110 (Sept. 11, 2000), FMLA-80 (Apr. 24, 1996) and FMLA-31 (Mar. 21, 1994).

Ownership of Employee-Authored Works

In general, the copyright ownership of a work initially vests in the author of the work. This means, for example that someone who writes the great American novel, a killer software application, or various other forms of expression, holds the exclusive right to publish the work, to make copies of it, and sell copies in the marketplace.

In the case of a work *made for hire*, U.S. copyright law states:

> the employer or other person for whom the work was prepared is considered the author . . . and, unless the parties have expressly agreed otherwise in a written instrument signed by them, owns all of the rights comprised in the copyright.

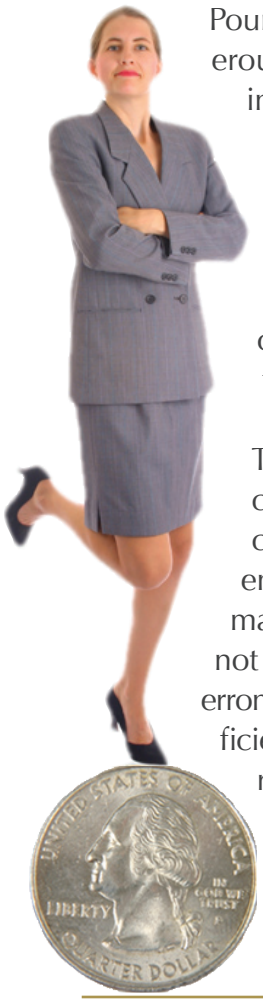
Ownership of works made for hire can be very important to an employer, since the work may contain trade secrets or other proprietary information, or it may be marketable as part of the employer's business. A recent case from the U.S. Court of Appeals for the Fifth Circuit is illustrative.

Pritchett, L.P. was a business consulting firm in Texas. In 1981 Pritchett hired Ronald Pound and had him execute an employment contract specifying

that should the Employee produce any written materials in the course of his work with the Employer, then such shall be done for and on behalf of the Employer and all work produced shall be the exclusive property of the Employer.

Pound was paid a salary plus a discretionary bonus, which reached $1 million the last year he worked for Pritchett.

In the late 1980s, Pritchett began offering a line of handbooks to supplement its consulting services. Pound and the owner of the business co-wrote two such books. Pritchett paid all expenses associated with the writing, marketing and promotion of the books and all revenues from sales of the books went directly to Pritchett. Pritchett also registered the books with the U.S. Copyright office, showing Pound as one of the authors, but it mistakenly checked "no" in answer to the question whether the books were works made for hire.



Pound died in 1995. Pritchett made numerous concessions to Pound's widow, including payment of Pound's full, $1 million bonus for 1995 even though Pound had only worked during the first quarter. Not satisfied with Pritchett's generosity, Pound's widow sued, alleging co-ownership of the books' copyrights and demanding royalties from the books' sales.

The Fifth Circuit rejected the widow's claim. It ruled that under both general copyright law and under the parties' employment contract, the books were made for hire, meaning that the employer, not Pound, owned the copyrights. The erroneous copyright registration was not sufficient, said the Court, to defeat the general rule that works made by an employee are considered made for hire.

References: 17 U.S.C. § 201; *Pritchett, L.P. v. Pound*, 2006 WL 3704859 (5th Cir. 2006).

Validity of Severance Agreements Prohibiting EEOC Charges

Suppose you terminate an employee under circumstances that seem entirely justified to you but which you fear might give rise to a claim of discrimination. One way to protect yourself is to offer the employee a severance package – say three months' additional salary, with benefits – in exchange for a full release of all claims he might have.

Naturally, you will want to make the release as comprehensive as possible. You might, for example, include not only a release provision, but also a provision that the employee will not file suit against you. Mindful that in addition to filing suit, the former employee could also file a charge of discrimination with the Equal Employment Opportunity Commission or a state or local fair employment practices agency, you might be tempted to expand the release to prohibit the filing of such charges as well.

But is an agreement not to file EEOC charges lawful? And if not, do you violate any discrimination laws simply by asking your former employee to sign such an agreement?

Virtually all the federal, state and local employment discrimination laws contain non-retaliation provisions that prohibit an employer from interfering with an employee's exercise of his or her rights under the discrimination law. Title VII, for example, makes it illegal to take adverse action against an employee

> because he has opposed any practice made an unlawful employment practice ..., or because he has made a charge, testified, assisted, or participated in any manner in an investigation, proceeding, or hearing.

The EEOC and the courts have long taken the position that an employee's rights under nondiscrimination laws are non-waivable, so that promises not to file a charge or participate in an EEOC proceeding are

null and void as a matter of public policy. This is so at least in part because the EEOC does more than just seek relief for individual victims of discrimination. The EEOC also has the broader responsibility of enforcing the civil rights laws generally. To do so, the EEOC may seek an injunction against future discrimination, it may require an employer to take general remedial measures for the benefit of whole groups of employees, and it may monitor an employer's compliance over a period of years.

In addition, according to the EEOC the very act of asking an employee to waive his charge-filing right is illegal. In a 1997 Enforcement Guidance, the EEOC said that an agreement which extracts such a promise from an employee may itself amount to a separate and discrete violation of the anti-retaliation provisions of the civil rights statutes. The U.S. Court of Appeals for the Sixth Circuit recently had occasion to consider that question.

Elizabeth Salsbury, a speech and language pathologist employed by Sundance Rehabilitation Corporation in Ohio, was terminated as a result of a reduction in force. She and all other terminated employees were offered a lump sum severance equal to 80 hours of pay provided they agree, among other things, not to file a charge with any administrative forum. According to the release agreement, if an employee signed the document, accepted the severance, and later filed a charge, the employee would forfeit the severance payment and have to refund it to the company.

Salsbury refused to sign the release, believing that she had been discriminated against because of her sex. The EEOC concluded that there had been no sex discrimination, but it also concluded that the very fact of the company's requesting her to sign the waiver provision amounted to illegal retaliation.

The Sixth Circuit disagreed with the EEOC. The Court acknowledged that the waiver provision was probably unenforceable, but that the mere offering of a severance agreement containing such a provision was not, of itself, unlawful.

References: EEOC Enforcement Guidance No. 915.002 (Apr. 10, 1997); *EEOC v. Cosmair, Inc.*, 821 F.2d 1085 (5th Cir. 1987); *EEOC v. Sundance Rehab. Corp.*, 466 F.3d 490 (6th Cir. 2006).

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

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By Charles H. Fleischer, Esq. Oppenheimer, Fleischer & Quiggle, P.C.

Are Your HR Policies Ready for the Flu Pandemic?

Experts tell us that Bird Flu – technically, Influenza type A virus, subtype H_5N_1 – is likely to mutate and become transmittable from human to human. When that happens, a pandemic will almost certainly occur. While we have seasonal flu every year, Bird Flu, if it strikes, will be much worse, more like the so-called Spanish Flu of 1918. This is so in part because Bird Flu is a new strain for which natural immunities do not exist, and in part because Bird Flu appears to trigger an overwhelming (and often deadly) immune response, called an inflammatory cascade or *cytokine storm*. In contrast to seasonal flu, which takes its greatest toll among the elderly, the very young, and others with compromised immune systems, Bird Flu is likely to take a significant toll on healthy young adults.

The effectiveness of antiviral treatments such as Tamiflu is uncertain and quantities are limited. While flu vaccines are likely to be effective, pro-duction cannot begin until the pandemic has actually started and the particular viral strain is identified. This means a delay of six months or more before a vaccine is available.

A Bird Flu pandemic is expected to come in three, more or less distinct waves over a period of approximately 18 months. We will probably get no more than six weeks' advanced notice from the time the pandemic has begun until it reaches the U.S. When it hits, businesses can expect absenteeism of 30% to 40%. Public health authorities may also take steps that limit commercial activity, such as restricting travel, shutting down mass transit, quarantining families when one family member is reported sick, prohibiting public gatherings, and closing schools. With schools closed, an employee-parent may have to stay home, too. Even healthy em-ployees who could otherwise get to work may be afraid to show up for fear of getting infected.

To survive a pandemic, businesses clearly need to do some serious continuity planning and they need to begin that planning now. This article focuses on the HR aspects of such a plan.

Employee Safety and Health – Limiting the Spread

The word *influenza* comes from the Italian, referring to unfavorable astrological influences which were first thought to be the cause of the illness. Influenza viruses that affect humans appear to be spread through coughing, sneezing and talking in close proximity, and by direct contact such as kissing. The viruses also live for many hours on surfaces such as desks, telephone handsets, and office equipment.

It makes good business sense for employers to take whatever steps they can to keep their workforce healthy. They may also have a legal obligation to do so under federal and state occupational safety and health laws,

which impose on all employers the general duty to furnish employment which is free from recognized hazards likely to cause death or serious physical harm.

This means limiting the spread by good sanitation practices and social distancing. For example, employers should:

- Educate employees as to means of transmission, symptoms, treatment, etc.
- Encourage frequent hand washing
- Suspend social customs like hand shaking
- Encourage employees to clean work areas frequently with alcohol wipes
- Provide and encourage use of hand sanitizers
- Provide and encourage use of face masks or respirators
- Spread employees out over work areas and stagger their shifts
- Cancel face-to-face meetings
- Require symptomatic or exposed employees to stay away from the workplace
- Implement a telecommuting policy for as many employees as possible
- Limit non-essential travel, especially to regions where flu is prevalent
- Isolate employees who are returning from flu-prevalent regions

A word about telecommuting. If you wait to implement a telecommuting policy until illnesses and absences start climbing, the policy is bound to fail. You must begin now to identify those employees whose duties and work habits make them good candidates for telecommuting and then require them to dedicate a space at home exclusively for work; pay for, install and test dedicated phone lines and high-speed internet connections; pay for, install and test communications software; and practice, by having employees work from home on a regular basis.

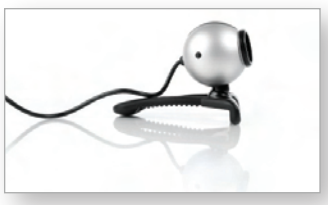
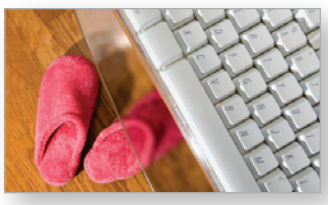
Critical Functions – Staying Afloat

When public health officials impose limitations on travel and public gatherings, and when significant numbers of customers are home sick, some industries will experience a downturn in business. Restaurants and movie theaters, for example, are likely to suffer a substantial reduction in revenue.

Other industries, such as public utilities, communications companies and supermarkets, will enjoy continued demand for their products and services, but they may find it difficult to operate with reduced staff. Still other industries will experience an increase in demand – hospitals, clinics, phar-macies and funeral homes come to mind.

The first step is predicting as accurately as possible the likely effect of a on your customers and therefore on your business. If you are in an industry that will face a downturn, perhaps you can provide a related product or service that will remain in demand. A restaurant, for example, might market carry-out and home delivery instead of on-site food service. A bank might expand its drive-through facilities or encourage electronic banking.



Particularly those businesses that will face constant or increased demand in the face of high absenteeism need to identify critical functions that *must* be performed; provide backup for those critical functions, such as cross-training of employees; and postpone or eliminate non-critical functions.

If your business is one that can switch to a related product or service, your employees will need to be trained in providing that product or service. In the restaurant example, expansion of home-deliveries will affect staffing – fewer waiters, but more delivery personnel. De-livery employees will need to learn safe food-handling practices and how to process credit card payments off-site.

Communications – Keeping in Touch

No business can operate when its employees are unable to communicate with one another. If your business normally relies on face-to-face communications, alternatives will need to be put in place.

Experience with recent disasters shows that land line and mobile telephone systems may either be down or unreliable due to overload. Alternative means of communication include:

- E-mail via computers and mobile devices
- Company intranets
- Virtual private networks ("VPNs")
- Text messaging (also called "SMS" for short message service) via mobile devices
- Instant messaging
- Voice over Internet Protocol ("VoIP")

Each of these systems needs to be put in place and tested *before* the pandemic hits. For example, if e-mail will be an important form of communication, employees' home e-mail addresses will have to be collected and distributed and listservs should be created and kept current.

A company intranet provides a simple and relatively inexpensive way to communicate company-wide information, such as whether the office is closed, whether only essential employees should report in, etc. In fact, the whole pandemic response plan can be posted there for easy reference. A company intranet can be nothing more than a password-protected page on the company's main website. The page could have a link from the main website, labeled "Employees Only", or it could be unlinked and be accessed using a previously distributed web address.

Leave and Pay Policies – Taking Time Off

When a pandemic strikes, employers will need to have policies in place for determining when to allow time off, how much time to allow, and whether leave is with or without pay.

Most employers have a sick leave policy of some sort, perhaps five or ten days per year with pay, which may be accumulated from year to year up to a fixed maximum. But a pandemic is likely to exhaust available sick leave because of the severity of the illness, resulting in the need for excess leave.

In addition, a employee who is symptomatic, who has been exposed to Bird Flu, or who has just returned from to a flu-prevalent region, should not report in, even if he or she is otherwise able and willing to work. Will this type of absence be counted as sick leave (assuming the employee is not able to work from home)? Employees

who themselves are not sick may need to stay at home to care for a sick family member, to be with a child whose school is closed, or to grieve for a flu-related death. Do these absences qualify as sick leave? Finally, employees may be unable to get to work due to restrictions imposed by public health authorities, or they may be too fearful to come to work. How will these absences be counted?

Practical considerations will influence leave policies. For example, granting leave with pay to employees who have been exposed but who are asymptomatic will encourage them to stay home. Of course, paying employees not to work has a downside as well, and businesses may be hard pressed to offer generous leave with pay while at the same time facing a reduct-ion in sales.

Legal considerations also influence leave policies. For employers with 50 or more employees, the Family and Medical Leave Act requires employers to grant up to 12 weeks' leave without pay to eligible employees who have a serious health condition themselves or to care for a family member with a serious health condition.

FMLA defines *serious health condition* as an illness, injury, impairment, or physical or mental condition that involves either inpatient care in a hospital, hospice, or residential medical care facility; or continuing treatment by a health care provider. U.S. Department of Labor regulations expand on this definition: for a health condition to qualify as "serious" and involve "continuing treatment" the employee must be incapacitated (unable to work) for more that three consec-utive calendar days and the condition must involve treatment two or more times by a health care provider.

DOL regs go on to say that, absent complications, the flu would ordinarily not qualify as a serious health condition. However, Bird Flu is likely to be much more serious than the seasonal flu the DOL probably had in mind. And at least one court case (from the U.S. Court of Appeals for the Fourth Circuit, which includes Maryland and Virginia) has said even seasonal flu can qualify. See "Fourth Circuit Says Flu Can Qualify for FMLA Leave," Employer Alerts, June 2001, p. 4.

Another legal consideration relates to the status of exempt employees. Under the Fair Labor Standards Act and DOL regulations, most white collar exempt employees (executives, administrators and professionals) must be paid on a *salary basis* of at least $455 per week. To qualify as salaried, the employee must generally be paid for the entire week if he or she works any part of that week.

There are several exceptions to full-week pay rule. One involves FMLA. When an employee has exhausted available sick leave with pay and is on unpaid FMLA leave, the employee need not be paid to preserve his or her exempt status. This is true even if the leave is intermittent – for example, if an employee and his or her spouse are taking alternate half-days off to care for a seriously ill child.

When FMLA does not apply, the rule gets more complicated. In general, an exempt employee need not be paid for *full-day absences for personal reasons, other than sickness or disability*. So if an employee is absent for one or more full days for some personal reason other than his or her own illness, the employer need not pay. Note, however, that the employer must pay for *partial day* absences for personal reasons. See "Exempt Employees and Weather-Related Absences," Employer Alerts, Winter 2006, p. 2.

Under this rule, if the employee is absent from work to care for a sick family member, for bereavement, or because he or she is fearful of coming to work, then the leave qualifies as personal. On the other hand, if the employer temporarily closes down, then the leave is not personal and the exempt employee must be paid. But what if the employer is open for business but the employee is unable to get to work due to travel restrictions imposed by public health authorities? Is that absence for "personal reasons" and therefore without pay, or must the employee be paid to preserve exempt status? There is no clear answer at this time.

If an employee has workplace contact with an infected customer or other employee and the employee becomes ill with the flu, does he or she have a workers' compensation claim? Workers' comp statutes cover

injuries and illnesses "arising out of and in the course of employment." All three local jurisdictions cover occupational diseases, but they don't cover the general run of illnesses that the public at large is exposed to.

The flu is not generally thought of as an occupational disease and it would therefore not trigger workers' comp benefits in most cases, even if the contagion occurred at work. However, health care workers – particularly those who are treating flu victims – may have good comp claims. In a recent Massachusetts case, an EKG technician employed by a hospital, who became ill from a flu shot administered by the hospital, was awarded workers' comp benefits. A similar result was reached in a recent Delaware case.

Yet another legal consideration involves the Uniformed Services Employment and Reemployment Rights Act. It is reasonable to expect that in a Bird Flu pandemic, employees who are reservists or in the national guard will be activated to help preserve order, enforce quarantines, etc. Such service members must be treated as on furlough, with entitlement to the same or an equivalent job when they return. See "Job Rights of Employees Called to Active Duty," EMPLOYER ALERTS, Nov. 2001, p. 1.

Overtime – a Costly Alternative

Facing significant absenteeism, employers may be tempted to have their remaining employees put in overtime. While exempt employees need not be paid extra for overtime work, requiring them to put in extra hours at what is bound to be a stressful time may be counterproductive.

Nonexempt employees do need to be paid for overtime. The rule, simply stated, is that if a non-exempt employee works more than 40 hours in any workweek, the employee must be paid time and a half for those additional hours. In this context, a workweek is a 168-hour period such as from Sunday at 12:01 a.m. to the following Saturday at midnight. (The employer gets to determine the workweek but the employer cannot keep changing it to avoid overtime pay obligations.)

Overtime pay is due is even if the employer's pay-days are bi-weekly or semi-monthly. In the example of an employer who pays every other week, suppose an employee works 50 hours in week #1 and 30 hours in week #2. Although the employee has *averaged* only 40 hours per week, the employer must still pay time and a half for the extra 10 hours worked in week #1.

Internet Resources

A number of websites offer helpful information and links, including:

- http://www.pandemicflu.gov
- http://www.osha.gov
- http://www.ems-solutionsinc.com
- http://en.wikipedia.org/wiki/Influenza
- http://en.wikipedia.org/wiki/h5n1

References: 29 U.S.C. § 2601 (FLMA); 29 C.F.R. § 825.114; 29 U.S.C. § 201 (FLSA); 29 C.F.R. § 541.0; DOL Op. Ltr. No. FLSA2005-46 (Oct. 28, 2005); *Miller v. AT&T Corp.*, 250 F.3d 820 (4th Cir. 2001); Md. Code, L&E § 9-101; Va. Code § 65.2-100; D.C. Code § 32-1501; *Case of Hicks*, 820 N.E.2d 826 (Mass.App. 2005); *E.I. Dupont De Nemours & Co. v. Faupel*, 859 A.2d 1042 (Del. Super. 2004); Kolata, Gina, *Flu: The Story of the Great Influenza Pandemic of 1918 and the Search for the Virus that Caused It.*

Romantic Partner Denied Wage Protection

Michelle Hirsch founded a dog-grooming business in Asheville, North Carolina, called "Hair of the Dog," which she owned and operated as a sole proprietorship. She later met and became romantically involved with Tammy Steelman and they soon began living together. Shortly thereafter, Steelman quit her job at a residential cleaning company to work at Hair of the Dog.

Over the next four years, Steelman and Hirsch worked side by side in the business, paying all their living and personal expenses from Hair of the Dog revenues. According to Steelman, the two intended to stay together for life and they saw their work together as a way to improve their economic future.

They did not enter into any compensation arrangement, but Hirsch sporadically issued paychecks to Steelman to substantiate the company's claim that for insurance eligibility purposes Steelman was on the payroll. Steelman also had a company-issued credit card, which she used to cover her day-to-day expenses. When the credit card bills came due, they were paid with company funds. Hirsch later testified that although she discussed making Steelman a partner in the business, she never did so and instead considered Steelman an employee of the sole proprietorship.

The couple eventually grew apart and Steelman left Hair of the Dog. When Hirsch became romantically involved with someone else, Steelman sued, claiming she was due wages for her work at the business and statutory damages under the Fair Labor Standards Act. The issue before the U.S. Court of Appeals for the Fourth Circuit (headquartered in Richmond) was whether Steelman was a true employee for FLSA purposes.

The Court began its analysis with the FLSA's definition of *employee*, which is "any individual employed by an employer." The Fourth Circuit described this definition as completely circular and explaining nothing. The Court then looked to the economic realities of the arrangement between Hirsch and Steelman.

The traditional employer-employee relationship, said the Court, is a bargained-for exchange of one person's money for the other person's labor. But that was not the case here. To the contrary, Stellman and Hirsch worked side by side for their mutual, long-term benefit; they did identical work; they both exercised supervision over company employees; they shared the risks and rewards of their joint venture; and they each had control over company funds, which they used to pay personal ex-penses.

For these reasons, the Court ruled that Steelman was not an employee for FLSA purposes and she was not entitled to any relief under the statute.

The result here makes good sense. But employers should be aware that courts have a tendency to find in favor of an employer-employee relationship, rather than a relationship of independent contractors or, as in this case, joint venturers. This is because the law offers substantial protections to employees that it does not offer to independent contractors or joint venturers, such as workers' compensation and unemployment insurance benefits, wage and overtime guaranties, the right to unionize, and protection against discrimination. Classifying a particular worker as an employee also means the worker may be eligible to participate in any group benefit plans sponsored by the employer, and it means the IRS is more likely to collect income tax on the worker's compensation.

It may be difficult to think in legalistic terms when a working relationship is also a romantic one, but Hirsch could have saved herself a lot of legal expenses if she and Steelman had agreed in writing that their working relationship was a partnership or joint venture, rather than employer-employee. Hirsch's apparent reluctance to make Steelman a part owner in Hair of the Dog could easily have been accommodated by naming Steelman a non-equity partner, meaning that Steelman could share in profits and losses, but she would not contribute any capital, she would not be entitled to any proceeds should the business be sold, and Hirsch would retain ultimate control of the business.

References: Fair Labor Standards Act, 29 U.S.C. § 201; *Steelman v. Hirsch*, 473 F.3d 124 (4th Cir. 2007).

Employer May Consent to Police Search of Employee Workspace

The Fourth Amendment to the Constitution prohibits the government from conducting "unreasonable searches and seizures." With few exceptions, this means that a police officer must first obtain a search warrant, issued by a judge based on probable cause, before the officer may conduct a search and seize evidence of a crime. Evidence obtained in violation of the Fourth Amendment cannot be used by the government in a criminal trial of the person from whom it was illegally seized.

The question recently addressed by the U.S. Court of Appeals for the Ninth Circuit (headquartered in San Francisco) is whether it is unreasonable for the government to enter an employee's locked office, open his computer case, and copy his hard drive, all without a warrant but with permission from the employer.

Frontline Processing, of Bozeman, Montana, processes on-line payments for companies that sell on the internet. Frontline owns all its workplace computers and its IT department routinely monitors internet usage of the computers. Frontline's employees are aware of the IT department's monitoring capabilities.

In early 2001, Frontline's internet service provider notified FBI Agent James Kennedy that a Frontline employee had accessed child pornography websites from a Frontline computer. Agent Kennedy investigated, first contacting Frontline's IT administrator, John Softich. Softich told Agent Kennedy that the company had the capacity to constantly monitor every employee's internet activity, that the company had monitored the computer of an employee named Brian Ziegler, and that Ziegler's computer had been used to access child pornography sites.

According to Softich, Agent Kennedy instructed him to make a copy of Ziegler's hard drive, which Softich did. To do so, he obtained a key to Ziegler's private office from a company official, he entered the office using the key, and he opening the computer's outer casing to gain access to the hard drive.

Shortly thereafter, Frontline's corporate counsel contacted Agent Kennedy and told him that Frontline would cooperate fully in the investigation. Corporate counsel also indicated that the company would volun-tarily turn over Ziegler's computer and that a search warrant would be unnecessary. The computer was in fact turned over to Agent Kennedy, along with the previously-made copy of the hard drive. FBI forensic examiners later discovered many images of child pornography.

A federal grand jury indicted Ziegler for receipt and possession of child pornography and for receipt of obscene material. In response, Ziegler filed a motion to suppress the evidence found on his computer, arguing that when Softich entered Ziegler's office and copied the hard drive he was acting on behalf of Agent Kennedy, and that Agent Kennedy in turn needed, but did not have, a warrant.

The trial court denied Ziegler's motion, ruling that the evidence could be admitted at trial. At that point, Ziegler pled guilty to one count of receipt of obscene material, conditioned on his right to appeal the ruling that the seized evidence was admissible. Based on Ziegler's guilty plea, the trial court sentenced him to two years of probation and a $1,000 fine.

On appeal, the Ninth Circuit held that Zielger had a legitimate expectation of privacy in his office, and it assumed for purposes of its decision that IT administrator Softich was acting on Agent Kennedy's behalf, as if Softich himself were a police officer. However, according to the Court, the search was not unreasonable within the meaning of the Fourth Amendment because Frontline retained control over Ziegler's office and computer and it gave consent to the search and seizure.

One irony here is Ziegler's decision to appeal. After all, his conviction was only for obscenity, not child pornography, and he only got probation and a modest fine, without jail time. His unsuccessful appeal did not increase the sentence, but it did result in a published court opinion, available on line and in law books for all to see. For most people, the added publicity would be far worse than the sentence itself.

Reference: *U.S. v. Ziegler*, 474 F.3d 1184 (9th Cir. 2007).

Deductions for Cash Shortages Doesn't Affect Exempt Status. In general, exempt employees - employees who don't get time and a half for overtime - must be paid on a salary basis. The U.S. Department of Labor has ruled that the salary basis requirement is met even if the employer imposes deductions for bad checks or other cash shortages from the bonus component of the exempt employees' compensation, so long as the employees continue to receive a fixed salary of at least $455 per week. DOL Op. Ltr. FLSA2006-24NA. See "FLSA's 'Window of Correction,'" EMPLOYER ALERTS, March 2003, p. 3.

Electronic Storage of I-9 Forms Permitted. I-9 forms, which employers must complete and retain for all new employees to assure the employees' eligibility to work in the U.S., may be stored electronically as well as in paper form. According to the U.S. Immigration and Customs Enforcement, electronic storage may be accomplished either by scanning a completed paper version of the form, or the form itself can be completed electronically. 8 U.S.C. § 1324a; U.S.I.C.E Fact Sheet Apr. 26, 2005, available at www.ice.gov/pi/news/factsheets/index.htm.

Handbook Violates Federal Labor Law.

The D.C. Circuit has upheld a National Labor Relations Board ruling that provisions of an employer's handbook violate federal labor law. The employer, Guardsmark, LLC, which provides security guard services, had rules prohibiting employees from registering work-related complaints with Guardmark's customers, prohibiting solicitation and distribution of literature while in uniform, and prohibiting fraternization with other employees both on and off duty. According to the NLRB and the Court, these rules tended to chill the employees' federal statutory right to engage in concerted activity to improve wages, hours and other terms and conditions of employment. Guardsmark, LLC v. N.L.R.B., 475 F.3d 369 (D.C.Cir. 2007). See "Confidentiality Clause May Violate Federal Labor Law," EMPLOYER ALERTS, Winter 2006, p. 2

Maryland Prohibits Social Security Numbers on Paychecks. Effective January 1 of this year, it is illegal for Maryland employers to print an employee's Social Security number on the employee's wage payment check, on the check stub, or on any notices that wages have been direct deposited or credited to an employee's debit card or card account. Md. Code, L&E § 3-502.

In this issue of EMPLOYER*ALERTS* . . .

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