Klein Zelman Rothermel

Report From Counsel

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EEO DEVELOPMENTS

§1981 Expanded to Prohibit Retaliation?

Recently, the United States Supreme Court held that §1981, a long-standing federal statute enacted to protect freed slaves, encompasses retaliation even though the text of that statute is silent as to such claims. *CBOCS West, Inc. v. Humphries,* ___ S.Ct. ___, 103 Fair Empl. Prac. Cas. (BNA) 481 (2008).

Plaintiff, Hendrick Humphries, an African-American former manager of a Cracker Barrel restaurant, brought this case against Cracker Barrel claiming that he was dismissed because of racial bias and as retaliation for certain complaints. Humphries filed suit against the company alleging race discrimination and retaliation under both Title VII and §1981. The Title VII claim was dismissed for technical reasons but the retaliation claim under §1981 was dismissed on the ground that §1981 did not permit retaliation claims. The Court of Appeals, however, reinstated the §1981 claim, finding that the statute did encompass a claim of retaliation.

Section 1981, enacted just after the Civil War, provides that "[a]ll persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts … as enjoyed by white citizens." Initially, the statute represented an immediate post-Civil War legislative effort to guarantee newly-freed slaves the same legal rights that other citizens enjoyed. The question for the Supreme Court here, however, was whether this language includes claims for retaliation despite failing explicitly to say so.

The court examined the pertinent interpretive history, including a 1969 case *(Sullivan v. Little Hunting Park, Inc.*, 396 U.S. 229 (1969)) which held that §1982 (an analogous provision) encompassed retaliation claims, subsequent appellate cases finding the same, and others construing §§1981 and 1982 similarly. In 1989 (*Patterson v. McLean Credit Union*, 491 U.S. 164 (1989)), however, the Supreme Court significantly limited the scope of §1981, finding that the words, "to make and enforce contracts" did not apply to conduct by an employer after a contract relation had been established.

Two years later, Congress weighed in on the matter, passing the Civil Rights Act of 1991. The new law, designed to supersede *Patterson*, added a subsection to §1981 which defined "make and enforce contracts" to include "the making, performance, modification, and termination of contracts, and the enjoyment of all benefits, privileges, terms, and conditions of the contractual relationship." An accompanying House Report confirmed that the new section included, among others, harassment, demotion, hiring, and retaliation.

The Court then proceeded to deny each of Cracker Barrel's arguments, concluding: (1) there was no need, in light of *Sullivan* and the legislature's language nullifying *Patterson*, for Congress to use the word "retaliation" or include an explicit anti-retaliation provision; (2) overlap with other statutes, particularly Title VII, is necessary; and (3) there is no need to limit §1981 to status-based discrimination (*i.e.*, who you are), and ignore conduct-based discrimination (*i.e.*, what you did).

The decision to include retaliation in the scope of activity prohibited by §1981 will not drastically affect most discrimination cases since a retaliation claim can also be brought under Title VII. However, plaintiffs will benefit by being able to assert retaliation claims

under §1981 (and employer exposure will be greater) because §1981 is more favorable to plaintiffs in several important respects, including: (i) §1981 covers all employers, while Title VII covers only employers with 15 or more employees; (ii) §1981 claims can be filed directly in court while Title VII requires first filing a charge with EEOC; (iii) there are no caps on compensatory or punitive damages under §1981, whereas Title VII includes such caps; (iv) individuals can be held personally liable under §1981 but not under Title VII; and (v) §1981 has a three-year statute of limitations while Title VII requires that charges must be filed within 300 days (in states with EEO protective laws).

Second Circuit: How Broad is the Concept of "Discrimination"?

The court of appeals in New York held for the first time that illegal discrimination has occurred when an employer takes disciplinary action against an employee because of that employee's association with a person of another race. *Holcomb v. Iona College, 521 F.3d 130 (2d Cir. 2007).* In that case, the plaintiff, who is white, claimed that the college's decision to terminate his employment as an assistant coach of its basketball team was motivated by his marriage to a black woman. The court found that there was evidence that the college's decision was in part based on the race of Holcomb's wife and, therefore, that Holcomb was the victim of unlawful discrimination under Title VII.

The lower court had ruled against Holcomb, relying on the text of Title VII, which prohibits discrimination against an individual "because of *such individual's race."* Because Holcomb was white, that court found that he was not discriminated against because of *his* race.

The court of appeals had a different interpretation of the same words. It rejected the lower court's "restrictive" interpretation of the statutory language because: "where an employee is subjected to adverse action because an employer disapproves of inter-racial association, the employee suffers discrimination because of the employee's own race."

This is an expansive and creative interpretation of the statutory language. It is now the law in the second circuit. How this issue is handled in other parts of the country remains to be seen.

The Ledbetter Fair Pay Act

A bill to overturn the Supreme Court's decision in *Ledbetter v. Goodyear Tire & Rubber Co., Inc.*, 127 S.Ct. 2162 (2007) failed to obtain the 60 votes needed to proceed. Failure on Congress to vote on this issue is not surprising since President Bush has vowed to veto the bill if passed. Nonetheless, this bill is interesting because it signals where the next Congress will likely go if it is controlled by a Democratic Congress and Senator Obama is elected President.

In *Ledbetter,* the Court rejected the approach of several circuit courts under which the time for filing a discrimination charge with EEOC begins to run each time a paycheck is issued based on the discriminatory conduct. (Title VII requires that discrimination charges be filed within 300 days of the discriminatory act or 180 days in states which have no anti-discrimination agency). For example, suppose an employee claims that his paycheck is lower than it should be because of discrimination which began eight years ago. Under the "continuing violation" theory, that employee can file a charge within 300 days of each paycheck even if the underlying act of discrimination occurred more than 300 days before the paycheck was received.

In *Ledbetter*, the Supreme Court rejected that theory and held that a discrimination claim is untimely unless the employee files a charge within 300 days of the time that he knew or should have known about the underlying act of discrimination. This decision outraged many in Congress. Under the continuing violation theory, if an employee filed a charge challenging an action that occurred, say, five years earlier and affected that employee's pay, that employee could not obtain damages for the time period more than 300 days before he filed his charge. But under the Court's *Ledbetter* decision, that employee was not just limited in the damages he could seek; he is precluded from suing because he failed to file a charge within 300 days of the act of discrimination. Many have argued that the Court's decision is unfair and inconsistent with the underlying purpose of Title VII because it, in effect, legalizes unchallenged discrimination after 300 days even though the effects of the discrimination are felt with each paycheck, and it prevents the EEOC and the courts from correcting that discrimination going forward.

We would anticipate prompt reconsideration of the bill to overturn Ledbetter in the next Congress and likely passage into law if the Democrats control Congress and Senator Obama is President.

ARBITRATION

Can Parties Expand the Reviewability of Arbitration Awards by Contract?

Practitioners of arbitration understand that court review of arbitration awards is very narrow. In the labor context, the Supreme Court held long ago that an arbitrator's award must be sustained in court unless the award does not derive its "essence" from the labor agreement. This is true even if the arbitrator made mistakes of fact or errors of law.

The Supreme Court has now decided the question of whether parties to a contract can expand the scope of judicial review by contract. *Hall Street Associates. LLC v. Mattel, Inc.*, 128 U.S. 1396 (2007). In that case, the arbitration agreement between the parties provided that a federal court could invalidate any arbitration award rendered under the contract if "the arbitrator's findings of fact are not supported by substantial evidence" or where "the arbitrator's conclusions of

law are erroneous." Normally, when a court reviews an arbitration award, the court could not overturn that award on either of these grounds. The issue in this case was whether the parties could expand the scope of judicial review by contract. Although this case arose in the commercial context, its logic would seem to apply in the labor/employment area as well.

Hall Street's main argument was that arbitration is a creature of contract, and, therefore, the parties had the right to define the scope of judicial review of any arbitration award issued under the contract. The Court rejected this argument. It noted that the Arbitration Act listed the specific grounds for vacating arbitration awards, for example, "corruption," "fraud," "exceeding powers." It reasoned that given "this emphasis on extreme arbitral conduct," a "statute with no textual hook for expansion" cannot be expanded by the parties to permit review of "just any legal error." As the Court found, "fraud and a mistake of law are not cut from the same cloth."

This decision reinforces the long-established rule that the parties are bound by arbitration awards even if they are erroneous factually and legally, unless they can show that the arbitrator exceeded his authority by, for example, deciding an issue not submitted to him or altering the language of the contract.

FAMILY MEDICAL LEAVE ACT

Loaned Employees

The labor/employment ramifications of leased employment arise in numerous contexts. A decision by the sixth circuit court of appeals addresses the issue under FMLA and sets out the criteria for determining when the leasing company will be liable for FMLA obligations of the employer to whom an employee was "leased." *Grace v. Uscar and Bartech Technical Services*, LLC, DLL, 3/27/08, sec E-1 (6th Cir. 2008).

The plaintiff in this case, Grace, was employed by a "leasing" company, DGE, which "leased" her to USCAR, where she worked for seven years. After Grace was hospitalized with a lung condition, she took FMLA leave. Before she applied for reinstatement, DGE went bankrupt. When Grace applied for reinstatement, she was told that her job had been eliminated by USCAR, and, therefore, she had no job to which she could return; and that DGE had been replaced with a different leasing company, Bartech.

Grace brought suit, claiming that because she was denied reinstatement, both USCAR and Bartech (as a "successor" leasing company) had violated FMLA. The interesting issues in this case are whether and when a leasing company and a "successor" to a leasing company are responsible for FMLA violations.

The court held that separate employers can be deemed a single "employer" for FMLA purposes under two different tests. The first test, the "integrated employer" test, looks at four factors: common management; interrelation between operations; centralized labor relations; and degree of common ownership. The second test, described as the "joint employer" test, assumes that two companies are legally separate but that "they have chosen to handle certain aspects of their employer-employee relationships jointly." This kind of relationship will typically arise when two companies share an employee's services or where "one employer acts directly or indirectly in the interest of the other employer in relation to the employee." The court found the second test to be relevant in this case, noting the Department of Labor regulations which say that joint employment will ordinarily be found to exist when a temporary or leasing agency supplies employees to a second employer."

The court then addressed the obligations of the two companies. It found that Bartech, the leasing company which succeeded Grace's initial employer, was the "primary" employer of Grace and that it was responsible for providing FMLA notices to employees. But when Grace actually took FMLA leave, both the "primary" and "secondary" employer (USCAR) were responsible for honoring Grace's decision and not retaliating.

The court noted the employers' defense that an employee is not entitled to reinstatement after FMLA leave if the employer shows that her job would have been eliminated regardless of whether she had taken that leave. However, the court found sufficient factual evidence to warrant a trial on that issue.

Bartech also invoked, as a defense, the requirement that employees must have worked at least 12 months before they qualify for FMLA leave. Bartech argued that while Grace had worked for DGE at USCAR for seven years, she had worked for Bartech (DGE's "successor") for only a few months. The court rejected that argument, applying an "equity" test which focuses on several factors: the interests of the employee; the interests of the employer; and the policies underlying FMLA. (A more subjective "test" would be difficult to find). Applying that test, the court found that the equities balanced in Grace's favor and, therefore, that she was an employee entitled to FMLA leave. As the court noted, the effect of denying FMLA coverage to Grace would be to deny coverage to an employee who had worked as a "loaned employee for the same employer (USCAR) for eight years."

This case illustrates one of the many vulnerabilities of "leased" employment. The company which obtains an employee from a leasing company cannot assume that that person is employed only by the leasing company, and it should understand that it, too, may have employment obligations to the "leased" employee.

Paid FMLA Leave

FMLA does not require paid leave, but employees may become eligible for paid leave under recent and pending

legislation. Currently, California is the only state in which employees receive paid FMLA leave, but New Jersey and Washington both have passed new laws (which take effect in 2009) granting paid FMLA leave. Movements to do the same have begun in New York, Massachusetts, Oregon and in Congress.

This does not mean that employers will be obligated to pay for the FMLA leave. In New Jersey, for example, the leave will be financed by employee pay deductions to establish a state-run fund which will pay for the leave.

GINA: FEDERAL PROTECTION AGAINST GENETIC DISCRIMINATION

President Bush has signed into law the Genetic Information Nondiscrimination Act (GINA). This law prohibits discrimination by employers or insurers based on an individual's genetic information. Rights under GINA are enforceable through EEOC and federal courts, and, like Title VII and disability claims, prevailing plaintiffs are entitled to legal fees, compensatory and punitive damages and back and front pay.

There are some differences. The caps on compensatory and punitive damages are $300,000 under GINA, slightly lower than in other EEO cases. Another difference is that GINA does not recognize disparate impact claims.

EEOC is required to issue enforcement guidelines with one year.

This will be an interesting subject to follow. It remains to be seen how much actual litigation results from this law given the fact that most employers do not use genetic discrimination in making decisions that affect their employees. Time will tell what the effect and parameters of this new law will be.

THE NY LABOR LAW NOW REQUIRES WRITTEN COMMISSION AGREEMENTS

In recent years, the New York State Department of Labor ("NYDOL") has found itself in the middle of numerous disputes regarding the earning and payment of commissions. In many of these disputes employees filed claims alleging that their employer failed to properly pay owed commissions. As a result, the NYDOL was placed in the tedious role of trying to figure out and understand the agreed upon commission structures. To alleviate this difficult situation, the New York State Legislature amended Section 191 of the New York Labor Law to impose new requirements on businesses that employ commissioned salespersons.

The Law and Requirements

As of October 16, 2007, all entities that employ commissioned salespersons must execute written commission agreements with their commissioned salespersons. A "commission salesperson" is broadly defined as an any individual who is engaged in sales and who is at least in part paid on commission.

The new law requires the employer and the commissioned salesperson to sign in writing and for the employer to retain a copy of the agreement for a three-year period. In addition to the above, the Labor Law now requires the written document to include certain language. More specifically, the new law requires the written commission agreement to describe the manner in which wages, salary, and draws against commissions will be calculated; the frequency of any reconciliation between a draw and earned commissions, and details regarding the payment of commissions upon termination.

In the event that the employer fails to reduce a commission agreement to writing as set forth above, the statute specifically provides that a presumption will be drawn in favor of the employee. In short, this means that the employee's overall understanding of the commission arrangement will likely be enforced. By failing to get these written agreements, employers run significant litigation risks if the manner in which they pay commissions is ever challenged in court or by the NYDOL.

Improper Wage and Hour Deductions and Written Agreements

On a related note, on June 10, 2008, the New York Court of Appeals rendered its decision in *Pachter v. Bernard Hodes Group, Inc.*, 2008 WL 23338595 (N.Y. 2008). This important decision affects all employers who compensate their employees on a commission basis and clarifies two disputed issues under Article 6 of the New York Labor Law.

The facts of the *Pachter* case are as follows: From April 2002 through December 2003, Elaine Pachter "Pachter") worked as a "vice-president" for Bernard Hodes Group, Inc. ("Employer") Pachter did not earn a salary; instead she was paid commissions. Specifically, Pachter earned a percentage of the amounts that she periodically billed; however her Employer deducted particular charges from these figures. The deductions included: (1) finance charges for late fees; (2) a percentage of the costs related to her assistant; (3) various expenses (including those related to entertainment); (4) errors; and (5) portions of the losses caused by clients she obtained that were unwilling and/or unable to pay for the services rendered. While this practice occurred for eleven years, there was never a written agreement between Pachter and her Employer memorializing the commission structure.

Shortly after her employment terminated, Pachter filed a lawsuit against her Employer alleging that these "deductions" were unlawful and that they violated section 193 of the New York Labor Law ("Section 193"). Section 193 (which is a subsection of Article 6) prevents employers from making certain deductions from employee "wages." Under Section 193, only deductions that are

authorized in writing and that are “for the benefit of the employee” are permitted.

Because of Pachter’s status as a “vice-president,” the Employer initially argued that Pachter was an “executive” and that her claims failed as a matter of law because she was not an “employee” covered by the protections set forth in Article 6. The Court rejected the Employer’s argument by finding that executives are “employees” for purposes of Article 6, except where expressly excluded. The Court reasoned that it would not be logical to include executives in some portions of Article 6 and specifically exclude them from others if they were not "within the ambit of the general definition of 'employee'."

As such, the Court decided that, despite her status as an executive, Pachter was entitled to the protections against the unlawful deduction of wages, as set forth within Article 6 of the New York Labor Law, and specifically within Section 193.

After rejecting this initial argument, the Court also examined the Employer’s secondary argument that the deductions did not violate Section 193 of the New York Labor Law because they were made prior to the commissions being “earned” by Pachter. The Court agreed with the Employer with respect to this argument. Specifically, the Court found that nothing in the Labor Law prevents employees and employers from contracting as to when a commission becomes "earned." The Court found that the parties are free to agree that the computation of a commission will include certain downward adjustments from gross sales, billings or receivables. Therefore, if the parties agree to such deductions, it will not be considered an unlawful deduction from "wages" because the parties have mutually decided that the wages have not yet become "earned."

However, as stated above, there was no written agreement between Pachter and the Employer detailing when her Commission would actually become earned. Notwithstanding, the Court found that the parties had entered into an implied contract based on their course of dealings over their eleven-year relationship. The Court took particular notice of the fact that the Employer issued written monthly compensation statements to Pachter, which detailed the various deductions and adjustments. The Court reasoned that Pachter understood the adjustments and acquiesced to them. As a result, the Court denied Pachter’s claims that the deductions from wages were unlawful.

Nevertheless, the Court indicated that the common law rules regarding commissions shall apply if there is no agreement. Under the common law, a commission becomes “earned” when the employee produces a “ready, willing and able purchaser of services.” With that said, if an employer pays its employees on a commission basis without an agreement to make certain deductions, the employer may be running afoul of New York’s wage deduction laws if it later makes adjustments to and/or deductions from those commissions. Without an agreement, it is much more difficult to argue that the commissions were not yet “earned.”

Considering the above, the lesson for employers who employ individuals on a commission basis is to get these commissioned agreements in writing. Based on the amendments to the Labor Law and to the decision in *Pachter*, having a written sales agreement is not only required legally; it is also the best way to protect your business.

KLEIN ZELMAN ROTHERMEL’s Report From Counsel is published periodically with the intent to inform readers of recent legal developments and issues. It is not intended, nor should it be used, as a substitute for legal advice or opinion which can be rendered only when related to specific fact situations.