



## NEW CONSIDERATIONS FOR SEVERANCE AGREEMENTS IN LIGHT OF IRS CODE SECTION 409A

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Counsel should be increasingly cautious when negotiating and reviewing severance agreements for adverse tax consequences. The landscape with respect to severance pay and benefit provisions has changed with the enactment of new regulations under Section 409A of the Internal Revenue Code governing the treatment of deferred compensation. The following discussion is intended to alert employment law practitioners, particularly those representing employees, to Section 409A provisions that may impact severance negotiations so that, when necessary, expert tax and/or employee benefits advice may be secured.

The American Jobs Creation Act of 2004 was signed into law on October 22, 2004. It created a new Section 409A of the Internal Revenue Code, effective January 1, 2005. This Section impacts nonqualified retirement plans and other deferred compensation arrangements, including “severance pay plans” or severance agreements.<sup>1</sup> Its purpose is to eliminate abuses, such as those taken by Enron executives, related to election timing, distribution timing, and the ability to receive accelerated payments. Section 409A’s final regulations, published on April 17, 2007, became effective on January 1, 2008. (72 FR 19234-01, 1.409A-1(b)(9)). See [www.ustreas.gov/press/releases/reports/td9321.pdf](http://www.ustreas.gov/press/releases/reports/td9321.pdf) for a full copy of the final regulations.

Section 409A, including its application to certain severance pay plans, is significant for two reasons. First, it regulates non-qualified deferred compensation through a number of complicated rules and regulations. Second, the rules impose harsh penalties in the event of non-compliance. For example, there is a 20% penalty tax *to the employee*, not the employer, on the particular payment or benefit that fails to comply with Section 409A and, in some instances, underpayment interest plus 1% (26 CFR 1.409A (a) (1) (B) (2005)).

On September 10, 2007, the IRS issued Notice 2007-78, providing plan sponsors an extension to December 31, 2008 to maintain compliance with written documentation relative to deferred compensation plans. However, *actual* compliance until that date has not been suspended. Therefore, this year is pivotal to ensure that employment contracts and other contractual provisions the employee has entered into with his or her employer are modified to comply with Section 409A. If those modifications have not been made in a timely fashion, penalties will result.

Given the complexity of Section 409A, for the purposes of this article and unless stated otherwise, it is presumed that the employee does not have a preexisting agreement with his or her employer regarding severance pay. In other words, at the time of separation from employment, there is a “clean slate” within which these negotiations commence.

**Legal Settlements.** It is important to recognize that *severance* agreements that are actually *settlement* agreements of bona fide legal claims are not considered deferred compensation under Section 409A (72 FR 19234-01, 1.409A-1(b)(11)). These claims may include those based on wrongful termination, employment discrimination, the Fair Labor Standards Act, or workers’ compensation statutes, irrespective of the law under which the claims arise and regardless of the status of the settlement proceeds as compensatory payments. The payment or reimbursement of attorneys fees incurred in connection with the resolution of these claims is also exempt from Section 409A application. Section 409A, however, will apply if the settlement changes the timing of payments of deferred compensation already subject to the regulation. Whether or not a bona fide legal claim exists is determined based on the particular facts and circumstances. Accordingly, the mere fact that a release is being executed by the employee does not mean that a severance agreement is free of Section 409A scrutiny.

**Separation Pay Constitutes Deferred Compensation Under Section 409A.** “Separation pay” is compensation received by the employee that is conditioned upon his or her separation from employment. Separation pay is distinguished from other compensation the employee could otherwise receive without separating from employment; *e.g.*, an amount also payable upon a change in control or as a result of an unforeseeable emergency. Section 409A applies to severance agreements where the employee acquires a right in one year (*i.e.*, it is no longer subject to a substantial risk of forfeiture),<sup>2</sup> but it is not paid until the next year. Illustrations include the following:

- **Example 1:** Employer promises to pay severance to the employee if she is terminated without cause. Unless one of the exemptions under Section 409A (addressed below) is applicable, this is “non-qualified deferred compensation,” and it must comply with Section 409A.
- **Example 2:** Employee does not have a binding right to severance, but the employer nonetheless pays executive severance upon her termination in the same taxable year as the termination. There is no deferral of compensation into a difference tax year. Therefore, Section 409A does not apply.
- **Example 3:** Employee stops performing service for the employer but is maintained on the payroll until the following year. The final regulations do not treat salary continuation as delaying the actual separation date for Section 409A purposes.

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- **Example 4:** Upon employee's termination, employer agrees to reimburse her county club dues and allow her to use the corporate plane for the next five years. This is considered "non-qualified deferred compensation" and must comply with Section 409A.

**Regulatory exceptions making certain payments outside the definitional scope of "deferred compensation"** under Section 409A. Simply because severance compensation is deferred to a later tax year does not mean that it is subject to Section 409A's purview. A few significant exceptions, which define certain payments as *not* being deferred compensation under Section 409A, are important to note.

**Short-Term Deferral Exception.** The "short-term deferral exception" places certain payments paid to an employee in the year following termination outside the scope of Section 409A. Specifically, the short-term deferral exception excludes compensation that is paid within 2.5 months of the end of either *the later of* the employee's calendar year (March 15th) or the employer's fiscal year (which may be other than a calendar year) in which the compensation became vested; *i.e.*, no longer subject to substantial risk of forfeiture. Payments made subsequent to the 2.5 month period remain subject to the exception if the delay in payment was either attributable to administrative impracticality or would have jeopardized the employer's solvency. It is important to note that the impracticability or insolvency must have been unforeseeable; additionally, payment must have been made to the employee as soon as it was reasonably practicable (72 FR 19234-01, 1.409A-1(b)(4)).

**Limited Pay Exception.** Another important exception is the "limited separation pay exception" or the "two times exception." This exception provides that severance pay made pursuant to an *involuntary* termination does not constitute deferred compensation if the following requirements are met:

- the aggregate payments do not exceed the lesser of two times the employee's annual compensation<sup>3</sup> or two times the Section 401(a)(17) limit (\$230,000 x 2 for 2008) (which includes the value of benefits); and
- all payments are made no later than December 31 of the second calendar year following the year of termination (72 FR 19234-01, 1.409A-1(b)(9) & (m)).

**An employee's decision to terminate employment for "good reason."** An employee's separation from his own employment for "good reason" may also be considered an involuntary termination. This is dependent upon a facts and circumstances analysis of the particular discharge scenario. The final regulations also established a "safe harbor" analysis. Under the safe harbor, among other things, the good reason termination must result from a material diminution in duties, pay or authority, a material change in job location, or any other action or inaction that constitutes a material breach of the terms of an applicable employment agreement. The safe harbor analysis requires that the employee declare the existence of the good reason condition within 90 days of the "good reason" event and provide the employer with a 30-day cure period. Further, the termination from service must occur within two years following the initial existence of a violation of one of the qualifying "good

reason” events. Finally, the amount, time and form of payment upon the termination is substantially identical to the amount, time and form of payment payable due to an employer-initiated involuntary termination (72 FR 19234-01, 1.409A-1(n)(2)).

**Stacking is allowed.** Section 409A’s regulations allow its exceptions to coverage to be used in combination or to be stacked. For example, if an employee receives severance under the short-term deferral exception, those amounts are not included in the limits established in the limited pay exception.

**Illustrations of the Two Primary Exceptions.** In the following illustrations, assume the following: (1) the employee, Julie, is involuntarily terminated on March 1, 2008 by her employer; (2) the employer is a private entity; (3) Julie’s annual compensation is \$300,000 as of March 1, 2008; and (4) Julie is paid \$600,000 in severance, payable in the scenarios set forth below:

- **Example 1:** Julie is paid \$600,000 in a lump sum on June 1, 2008. Result: The lump sum is not subject to Section 409A consideration because it is not deferred compensation as it was paid in the same calendar year as Julie’s termination.
- **Example 2:** Julie is paid in five installments of \$120,000 each on the following dates: June 1, 2008, December 1, 2008, January 1, 2009, February 1, 2009, and March 1, 2009. Result: The first two installments are not deferred compensation as they were paid in the year of her termination. The remaining three installments are not considered deferred compensation either because they were paid out on or before March 15 or they are exempted under the short-term deferral exception.
- **Example 3:** Julie is paid in five installments of \$120,000 each on the following dates: June 1, 2008, March 1, 2009, June 1, 2009, July 1, 2009, and August 1, 2009. Result: None of the payments are considered deferred compensation under Section 409A. The first three installments were either paid in the year of termination or are subject to the short-term deferral exception. The remaining three payments are exempted under the limited pay exception because (1) Julie was involuntarily terminated; (2) the three payments total \$360,000, making it less than the applicable limit of \$460,000 (the maximum given that two times Julie’s annual income would be \$600,000) and (3) the payments were made prior to December 31, 2009.
- **Example 4:** Julie is paid in five installments of \$120,000 each on the following dates: March 1, 2009, April 1, 2009, May 1, 2009, June 1, 2009, and July 1, 2009. Result: The first installment is exempted under the short-term deferral exemption. The remaining four installments are covered by the limited pay exception, subject to the \$460,000 cap. However, because the last four installments total \$480,000, \$20,000 would be subject to Section 409A scrutiny. This amount is probably not subject to penalty provisions if paid pursuant to a fixed schedule.
- **Example 5:** Julie is paid in five installments of \$120,000 each on the following dates: April 1, 2009, May 1, 2009, July 1, 2009, August 1, 2009, and February 1, 2010. Result: \$20,000 of these payments made in 2009 exceeds the cap under the limited pay exception. Further, the last installment is outside the applicable time period for the limited pay exception. Accordingly, \$140,000 of Julie’s separation

compensation would be subject to Section 409A. As with the prior example, this would likely not be subject to Section 409A’s penalty provisions.

**Six-month wait provision for key employees of publicly traded companies.** Another significant provision of Section 409A is the six-month waiting provision for some executives of publicly traded companies (including a company whose stock is traded on a foreign stock market). Section 409A mandates a six-month delay in the payment of deferred compensation to “key employees” of these companies following termination from employment. In general, key employees are defined as the top 50 officers in the company who earn in excess of \$150,000 (indexed for 2008). Key employees are also those who are 5% owners or 1% owners having annual compensation greater than \$500,000 (26 USC 416(i)). Significantly, if a key employee’s severance arrangement meets an exemption, such as the limited pay exception, the payment does not have to be delayed for six months because it is not deferred compensation pursuant to the final regulations.

**Fixed Schedule Severance Arrangements.** In general, *voluntary* severance arrangements are subject to Section 409A. The final regulations address “permissible payments” under Section 409A, including those made to an employee upon a “separation from service,” whether voluntary or involuntary (72 FR 19234-01, 1.409A-3). Payments that are objectively determinable, nondiscretionary, and made pursuant to a fixed schedule are permitted. An example delineated in the regulations allows for “a schedule of three substantially equal payments payable during the first three taxable years following the taxable year in which a separation from service occurs.” Another IRS “clear as mud” example illustrates that while the payment amount does have to be specified, it must be nondiscretionary:

- Employee D provides services as an employee of Employer W, but is not a specified employee [subject to the six-month wait period]. Employee D participates in a nonqualified deferred compensation plan providing for 10 installment payments payable on the first 10 anniversaries of the date Employee D separates from service, provided that no installment payment in any year may be more than 1% of Employer W’s net income for the previous calendar year, and provided further that the excess over such limit that would otherwise be payable but is not paid due to application of the limit will become payable as of the first installment payment date at which time such amount, in combination with any installment payment otherwise due Employee D, does not exceed 1% of Employer W’s net income for the previous calendar year. Provided that Employee D does not retain effective control of the calculation of Employer W’s net income or the amount that Employee D will not be paid due to application of the limit, the plan provides for a schedule of payments upon a separation from service that complies with this section.

**Section 409A’s Application to More than Simple Severance Pay.** Section 409A does not exclusively apply to the actual dollars given to the employee upon termination. It also applies to equity compensation such as stock and in-kind benefits (*e.g.*, the use of an automobile). As with actual pay, the final regulations provide several exclusions from Section 409A coverage. The following examples are illustrative:

- Health benefits tied to the 18-month COBRA period;

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(Continued from page 3)

- Post-separation group-term life insurance coverage;
- Reasonable moving and relocation expenses;
- Outplacement services;
- Educational assistance;
- Indemnification provisions or the purchase of liability insurance;
- in-kind benefits and service payments on behalf of the employee (as long as the expense is incurred by or the benefits are provided by the end of the second year after termination and the payment is made by the end of the third year); and
- Miscellaneous fringe benefits that do not exceed the amount of Code Section 402(g) limits (\$15,500 in 2008).

**Conclusion.** The rules pertaining to Section 409A's application are extremely complex and interpretations are evolving. Indeed, the IRS had to provide employers with an additional year within which to bring their written plans into compliance with its regulatory requirements. It is imperative for employment counsel to be able to spot Section 409A issues in the drafting stage in order to avoid unintended penalties that could substantially and negatively impact the intent of a negotiated agreement.

— END NOTES —

<sup>1</sup>Section 409A does not apply to plans qualified under Code Section 401(a), such as 401(k) plans; annuity plans under Section 403(a); SEP or SIMPLE IRA plans under Sections 408(k) or (p); bona fide vacation, sick leave, compensatory time, disability or death benefit plans; annuity contracts of educational institutions, churches and tax-exempt charitable organizations under Section 403(b); and eligible deferred compensation plans of governmental employers and tax-exempt organizations under Section 457(b).

<sup>2</sup>A substantial risk of forfeiture exists if the entitlement is conditioned on the performance of substantial future services or the occurrence of a condition related to the purpose of the compensation and the possibility of forfeiture is substantial. 72 FR 19234-01, 1.409A-1(d)(1). A substantial risk of forfeiture does not exist when payment is contingent upon the execution of a release or consent to a non-compete.

<sup>3</sup>The "annual compensation" is not clearly defined in the final regulations. Counsel should consider this to include base salary as well as any bonus compensation that is regular and/or almost certain to be paid. ■

## SPRINT/UNITED MANAGEMENT v. MENDELSON: RETURN TO SENDER

C. John Holmquist, Jr.  
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### *Sprint/United Management v. Mendelsohn:* Return to Sender

When the United States Supreme Court granted the employer's petition for cert, the employment bar anticipated a decision resolving the status of "me, too" evidence in employment discrimination cases. The decision did not settle the issue.<sup>1</sup> While the Supreme Court stated that such evidence is neither *per se* admissible nor *per se* inadmissible, it vacated the Tenth Circuit's decision with instructions to have the district court clarify the basis for its evidentiary rulings under the applicable federal rules.<sup>2</sup>

### The Court's Decision

The issue that was presented to the court was whether a district court must admit "me, too" evidence from non-plaintiffs alleging discrimination at the hands of persons who played no role in the adverse employment action challenged in the case. The evidence which plaintiff sought to introduce consisted of the following:

- Testimony of five other Sprint employees who claimed their supervisors had discriminated against them because of age.
- Testimony of three employees who alleged that they heard one or more Sprint supervisors or managers make remarks denigrating older workers.
- Testimony of one employee who claimed that Sprint's intern program was a mechanism for age discrimination and that she had seen the spreadsheets suggesting that a supervisor considered age in making layoff decisions.
- Testimony of an employee that had been given an unwarranted negative evaluation "banned" from working at Sprint because of his age, and that he had witnessed another employee being harassed because of her age.
- Testimony of an employee who would testify that Sprint had required him to get permission before hiring anyone over the age of 40; and after his termination, he had been replaced by a younger employee; and that Sprint had rejected his subsequent applications.<sup>3</sup>

None of the proposed witnesses worked with plaintiff, and none worked for the supervisors in the chain of command who made the decision concerning the plaintiff.

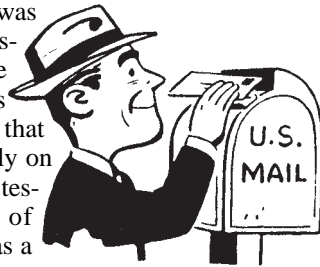
Sprint filed its motion in limine to exclude the testimony arguing that it was irrelevant to the case under Federal Rule of Evidence 401 and that the probative value of such evidence would be substantially outweighed by the danger of unfair prejudice, confusion of issues, undue delay, and misleading of the jury under Rule 403. The district court did not issue a written opinion but granted the motion in a minute order excluding evidence of discrimination against employees not similarly situated to the plaintiff. In defining "similarly situated employees," the district court stated that for purposes of its ruling, there must be proof to establish that the supervisor of Mendelsohn was the decision maker in any adverse

## WRITER'S BLOCK?

You know you've been feeling a need to write a feature article for *Lawnotes*. But the muse is elusive. And you just can't find the perfect topic. You make the excuse that it's the press of other business but in your heart you know it's just writer's block. We can help. On request, we will help you with ideas for article topics, no strings attached, free consultation. Also, we will give you our expert assessment of your ideas, at no charge. No idea is too ridiculous to get assessed. This is how Larry Flynt got started. You have been unpublished too long. Contact *Lawnotes* editor Stuart M. Israel or associate editor John G. Adam at Martens, Ice, Klass, Legghio & Israel, P.C., 306 South Washington, Suite 600, Royal Oak, Michigan 48067 or (248) 398-5900 or israel@martensice.com.



employment action and that there was temporal proximity. At trial, the district court orally clarified its minute order and stated that its order was meant to only exclude testimony that Sprint treated other people unfairly on the basis of age but would not bar testimony going to the question of whether the reduction-in-force was a pretext for age discrimination.<sup>4</sup>



"Return to sender!"

The Supreme Court stated that the Tenth Circuit had treated the minute order as a *per se* rule that evidence from employees with other supervisors was irrelevant in an age discrimination case. The Tenth Circuit found that the evidence was relevant and not unduly prejudicial and reversed and remanded for a new trial.

The Supreme Court first held that the court of appeals erred in concluding that the district court had applied a *per se* rule. Instead, the Court stated that given the circumstances of the case and the unclear basis of the district court's decision, the court of appeals should have remanded the case to the district court for clarification. In reviewing the minute order from the district court, the Supreme Court stated that the court of appeals' conclusion was unsupported by the order, since the order included no analysis suggesting that the district court had applied a *per se* rule excluding this type of evidence. Therefore, it was improper for the court of appeals to presume that the lower court reached an incorrect legal conclusion when the district court's language was ambiguous. The Court stated that questions of relevance and prejudice are for the district court to determine in the first instance. With respect to evidentiary questions in general, and Rule 403 in particular, the Court stated that a district court "virtually always" is in the better position to assess the admissibility of the evidence in the context of the case before it. The Court stated that relevance and prejudice under Rules 401 and 403, are determined in the context of the facts and arguments in a particular case, and as such, are not generally amenable to broad "*per se*" rules.<sup>5</sup>

The Court reviewed its position that because of a district court's familiarity with the case and its "greater experience" in evidentiary matters, courts of appeals are to afford broad discretion to the district court's evidentiary rulings. This discretion is especially true with respect to Rule 403 since the district court must make "on-the-spot balancing of probative value and prejudice . . ." which may lead to the exclusion of evidence found factually relevant because it is unduly prejudicial.<sup>6</sup>

In dicta, the Court stated that whether evidence of discrimination by other supervisors in an individual age discrimination case is relevant is a matter based on fact and depends upon many factors including how closely related the evidence is to the plaintiff's circumstances and the theory of the case. Applying Rule 403 to determine whether evidence is prejudicial requires a fact-intensive, contact-specific inquiry.<sup>7</sup>

### Decisions applying *Mendelsohn*

A post-*Mendelsohn* decision raises the interesting possibility that "me, too" evidence will be used by defendants. In *Elion v. Jackson*,<sup>8</sup> an African American female employee who had filed a Title VII action alleging race, gender discrimination, and retaliation, sought to exclude evidence of certain witnesses to be submitted on behalf of the defendant. The court allowed a white female employee to offer "me, too" testimony as to the defendant's favorable treatment of her. The district court stated that "me, too" evidence of an

employer's past non-discriminatory and non-retaliatory behavior may be relevant since an employer's favorable treatment of other members of a protected class could create an inference that the employer lacks discriminatory intent.<sup>9</sup> The court concluded the testimony is relevant and admissible under Rule 401 to the extent the testimony is offered to negate the inference that defendant harbored discriminatory or retaliatory intent. The court also determined that the testimony of an African American female employee was admissible. It concluded that the witness's testimony, to the extent that it was offered to negate the inference that defendant harbored discriminatory and retaliatory intent, is relevant and admissible. The witness, like the plaintiff, is an African American female. She was promoted to a director's position within four months of the reassignment of the plaintiff. As a result, under the circumstances of the case, her testimony may have significant probative value with respect to whether defendant harbored a discriminatory intent towards the plaintiff. The court stated that it could not perceive any danger of unfair prejudice, confusion or waste of time in permitting this testimony.<sup>10</sup>

In *Sgro v. Bloomberg*,<sup>11</sup> plaintiffs brought age, disability discrimination, sex, and retaliation claims under state law. The employer filed a motion for summary judgment which the court granted. The employees attempted to use testimony from a former employer that his supervisor systematically eliminated older employees by stating that they did not fit in. The court stated that the testimony was irrelevant while acknowledging that under *Mendelsohn* such testimony is not automatically foreclosed. There was no indication that this supervisor had any connection to the plaintiffs or their supervisors. Without such a showing, the supervisor's alleged discriminatory practice is simply immaterial to the court's determination whether the reasons offered by the defendant were a pretext for discrimination. The court stated that the plaintiffs had the opportunity for discovery and had come up short.

In *Opsatnik v. Norfolk Southern Corp.*,<sup>12</sup> the plaintiff sued his employer and union for age, sex and race discrimination. The court granted summary judgment to both defendants. In support of his case, plaintiff offered evidence as to comparably situated employees. The court noted that the employees did not work in the same department nor were they disciplined by the same decision makers. The court agreed with the plaintiff that under *Mendelsohn*, there is no *per se* "same supervisor" rule in the similarly situated analysis but disagreed that the identity of the supervisor was irrelevant to the case. The discipline imposed by other supervisors in other divisions does not speak to whether the plaintiff's supervisors acted with discriminatory intent.

In *Jones v. United Parcel Services*,<sup>13</sup> the district court reviewed the defendant's motion in limine in a retaliatory discharge case based upon state law. Plaintiff planned to call a former manager as one witness. The witness would testify about company policy and conversations with other managers concerning the treatment of injured or disabled employees and the company's directive to target, harass and terminate such employees. In addition, the witness would testify about his own treatment by the company over his attempts to return to work, including his successful litigation against the company. Citing *Mendelsohn*, the court stated that whether this is admissible evidence is fact based and dependent upon many factors and that it would be better able to make this determination in the context of evidence presented at trial. The court instructed counsel to approach the bench before presenting testimony regarding this witness.

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### **Analysis**

Are there any winners? Clearly, Federal District Court judges who explain, in writing, the reasons for evidentiary decisions are winners in light of the Supreme Court's admonition to the courts of appeals. The Court instructed the appellate courts that if they are in doubt as to the basis of a district court's decision because of ambiguous language, they are not to presume that the basis reached by the district court is based on incorrect legal conclusion but rather, are to remand it for explanation. In addition, the appellate courts are not to second guess the district courts by assessing the relevancy of the evidence on their own and by balancing the probative value versus prejudicial effect. A district court which explicitly makes the determination as to issues under Rule 401 and 403 and explains the basis for the decision, would be entitled to significant deference since, as the Supreme Court noted, with respect to evidentiary questions, and in particular Rule 403 questions, the district court is "virtually always" in a better position than the court of appeals to make that determination.

Although the Court's decision did not resolve the underlying issue of admissibility, the case has certainly created heightened awareness of the existence of and potential impact of "me, too" evidence. The Supreme Court's statement that "me, too" evidence is neither *per se* inadmissible nor *per se* admissible is of increased importance in motions of limine. It will be up to the district court to sort out the relevancy issues under Rule 401 and to balance the evidence with potential prejudicial effect under Rule 403. The parties should not expect to have these ruling overturned on appeal.

*Mendelsohn* is an evidence case which arose in the context of a discrimination claim. In light of the Supreme Court's decision, which did not resolve the issue of the admissibility of "me, too" evidence, the battle ground will be in discovery as plaintiff's continue to seek information regarding other employees and as employer's attempt to limit inquiries to individuals who had the same supervisor. The emphasis of the parties will be in maximizing the probability that the evidence developed in discovery will support their position with respect to admissibility under Rules 401 and 403.

— END NOTES —

<sup>1</sup>*Sprint/United Management Co. v. Mendelsohn*, \_\_ vs. \_\_, 128 S.Ct. 1140, 102 FEP Cases 1057 (2008)

<sup>2</sup>As is reflected in the title of this article, the Supreme Court's decision can be summarized to the tune of "Return to Sender" (with apologies to Elvis):

Sent my petition to the Supreme Court,  
Mailed it Special "D."  
Right after oral argument,  
They sent it back to me.  
They wrote upon it,  
"Return to Sender."  
Never should have been here,  
Don't know what we were thinking,  
Not our job to make it clear.

<sup>3</sup>128 S.Ct. at 1143

<sup>4</sup>128 S.Ct. at 1144

<sup>5</sup>128 S.Ct. at 1146

<sup>6</sup>128 S.Ct. at 1145

<sup>7</sup>128 S.Ct. at 1147

<sup>8</sup>— F. Supp 2d—, 2008 WL 921854 (D.D.C. 2008)

<sup>9</sup>Slip Op p. 7

<sup>10</sup>*Id.*

<sup>11</sup>— F. Supp 2d—, 2008 Westlaw 918491(D. N.J. 2008)

<sup>12</sup>— F. Supp 2d—, 2008 Westlaw 763745(W.D. Pa. 2008)

<sup>13</sup>— F. Supp 2d—, 2008 Westlaw 833480(D. Kan. 2008) ■

## **AUDITING FLSA PRACTICES: ENSURING THAT EMPLOYEES ARE PROPERLY CLASSIFIED AND COMPENSATED**

**Margaret Carroll Alli**

*Kienbaum Opperwall Hardy & Pelton, P.L.C.*

The federal Fair Labor Standards Act (FLSA), 29 U.S.C. 201, et seq., imposes minimum wage, overtime pay, recordkeeping, equal pay, and child labor requirements on most employers. Litigation under the FLSA has grown dramatically in recent years — especially class actions, which the FLSA calls "collective actions." 29 U.S.C. 216(b). Given this trend, employers would be well advised to take affirmative steps to strengthen their "good faith" defense to potential FLSA claims. 29 U.S.C. 259, 260.

The first step is to examine the organization's exempt classifications, payroll practices, complaint mechanisms, and training programs to make sure they meet applicable standards. An employer's reliance on U.S. Department of Labor (DOL) opinion letters may demonstrate good faith, as does reliance on the opinions of qualified experts such as compensation consultants or legal counsel. *Garcia v. Allsup's Convenience Stores, Inc.*, 167 F.Supp.2d 1308 (D.N.M. 2001). "Process" matters a great deal in employment law, and an organization that maintains active compliance efforts and reacts responsibly to workplace complaints may minimize potential liability. *Marshall v. Brunner*, 668 F.2d 748 (3rd Cir. 1982). Employers should also carefully investigate state wage and hour laws because many states, particularly California, have wage and exemption requirements that are more favorable to employees than FLSA rules and would therefore take priority. 29 U.S.C. 218.

### **The FLSA "White Collar" Exemptions.**

Generally speaking, employees must be compensated for all hours worked over 40 in a workweek at an overtime rate of one and one-half times their "regular" rate of pay. 29 U.S.C. 207(a)(1). Certain categories of workers are exempt from these overtime provisions, but these exemptions are narrowly construed and the employer must prove that overtime pay was properly denied. *A.H. Phillips, Inc., v. Walling*, 324 U.S. 490 (1945). The most common exemptions — the so-called "white collar" exemptions — apply to executive, administrative, and professional employees. 29 U.S.C. 213(a)(1). Assuming these employees receive a salary of at least \$455 per week and meet the regulatory definitions for "duties" and "salary basis," they do not have to be paid overtime for hours worked over 40 in a week because their salary is intended to cover all of their working time. 29 C.F.R. 541.602.

If an employee is misclassified as exempt, though, the employer may be liable for substantial back pay for unpaid overtime, liquidated damages (i.e., double back pay), damages for "willful" violations, and civil penalties, and may be subject to injunctions and other relief. 29 U.S.C. 216(b). The statute of limitations

is either two or three years, depending on whether the violation was “willful.” 29 U.S.C. 255(a). Managers or supervisors may be individually liable. *Bergstrom v. Univ. of New Hampshire*, 943 F.Supp. 130 (D.N.H. 1996). Additionally, if an employer maintains a policy that results in impermissible salary dockings, or otherwise treats employees in a manner inconsistent with salaried exempt status, scores of employees can be found to be non-exempt and entitled to unpaid overtime and other damages. 29 C.F.R. 541.603; *Baden-Winterwood v. Life Time Fitness*, 2007 WL 2029066 (S.D. Ohio 2007). To reduce the risk of such unpleasant surprises, the DOL added a “safe harbor” provision to the 2004 revisions to FLSA regulations, allowing employers to preserve the overtime pay exemption by implementing a “clearly communicated policy” prohibiting improper salary docking and including a written complaint mechanism that employees could invoke. 29 C.F.R. 541.603(d).

### Tips For Auditing FLSA Classification Practices.

#### 1. In general.

The following initial inquiries may be useful in assessing an organization’s FLSA compliance:

- Is a particular individual within the organization responsible for monitoring DOL opinion letters and legal developments regarding wage and hour issues?
- Who initially determines whether a position is classified as exempt or non-exempt? Is there an internal process with higher level review?
- Are managers trained concerning FLSA requirements, particularly the salary basis rule and internal complaint mechanisms?
- Are employees required to adhere to a regular schedule? Is that expectation in writing?
- Does the organization keep a record of time worked by employees, exempt and nonexempt, through timesheets or “electronic touches,” such as gate or hand swipes?

#### 2. Are employees properly classified as exempt or non-exempt?

In auditing whether employees perform exempt-type duties and are properly classified as exempt from overtime pay, an organization should consider the following:

- Are job descriptions, profiles, and employee self-evaluations reviewed? Do they accurately reflect the primary duties of the position?
- Do annual performance evaluations reflect exempt work? Do employees sign their evaluations to acknowledge the job duties expected of them?
- Are managers questioned to ensure that the job duties actually performed by employees meet the FLSA requirements to be exempt?
- Are the employees whose duties are at issue (or an appropriate sample) interviewed at regular intervals?

#### 3. Are the special rules for payment “on a salary basis” followed?

In determining whether an organization has adequate safeguards to protect the FLSA salary basis requirement for exempt white collar employees, the following inquiries may be helpful:

- Does the organization have a written policy prohibiting improper salary deductions (such as deductions for partial-day absences that are not otherwise unpaid FMLA leave)?
- Does the automated payroll system have electronic alerts to prevent impermissible salary docking?
- Is there a written “safe harbor” policy? Does it call for investigating pay complaints and timely reimbursing employees for improper deductions?
- Is there an automated system for requesting time off (paid or unpaid)? What are the review levels? Are there rules governing unpaid time off and, if so, is the unpaid time off limited to full-day increments?
- Are employee pay stubs or earnings statements understandable as to how compensation is calculated? For salaried exempt employees, do they reflect a predetermined salary that is regularly paid?

#### “Regular Rate Of Pay” Issues.

Another issue that is expected to be litigated with increasing frequency is whether an employer has correctly determined an employee’s “regular rate of pay” used in the overtime calculation. 29 U.S.C. 207(e). For example, DOL interpretive regulations require attendance bonuses and non-discretionary bonuses that induce employees to work more steadily or efficiently to be included in determining the employee’s regular rate of pay before overtime pay is calculated. 29 C.F.R. 778.211(c). In fact, all compensation that constitutes “remuneration for employment” must be included unless it falls within a specific statutory exception. 29 U.S.C. 207(e). A recent settlement between the DOL and a major retailer of allegations that the retailer had failed to include certain non-discretionary payments before computing overtime has increased interest in the “regular rate” issue, and the DOL has hinted that it may pursue future cases of this type.

#### Auditing Other Areas for Compliance.

In addition to FLSA issues, other Human Resource areas that may warrant systematic review include: independent contractor classification, FMLA practices, internal complaint and investigation procedures, disparate impact problems, and record retention issues (now receiving heightened attention as a result of the new federal rules on “e-discovery” in litigation).

Given the complexities of today’s employment rules, and the desirability of maintaining confidentiality through the attorney-client privilege, an organization should undertake careful planning with the advice of experts and legal counsel before beginning any compliance audit. ■

# MANAGERS AND SUPERVISORS NOT ALWAYS EXEMPT FROM OVERTIME PAY REQUIREMENTS

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The Fair Labor Standards Act (“FLSA”) requires employers to pay overtime to any employee who works more than 40 hours in a work week, unless that employee falls within one of the specific exemptions to the overtime requirement. One category for exemption is known as the “executive” exemption. Employers often assume that if someone has the title of supervisor or manager, they are automatically considered to be exempt as an “executive.”

This assumption does not always hold true. The Department of Labor’s (DOL) regulations give very specific criteria for an employee to qualify as an exempt executive. The primary duty must be the management of an enterprise, department or subdivision of the organization. In addition, the executive employee must regularly direct the work of at least two other employees. The direction of work of other employees must include either the full authority to hire and dismiss employees supervised, or giving a recommendation regarding hiring and dismissal that is given particular weight by another decision-maker.

This analysis depends upon employees’ actual job duties, not just their title. Generally, exemptions from FLSA coverage are narrowly construed by the courts. FLSA overtime exemptions are “affirmative defense[s] on which the employer has the burden of proof.”<sup>1</sup>

RadioShack recently agreed to pay out \$8.8 million to settle a group of lawsuits involving a demand for overtime by its store managers.<sup>2</sup> A federal district court judge had held in 2005 that RadioShack’s managers were entitled to overtime pay because they did not spend at least 80% of their time supervising other employees. In contrast, a federal court in Pennsylvania had ruled in favor of RadioShack on similar claims.<sup>3</sup> Based on their work of 50 or more hours per week, this group of managers will receive the back pay owed then for two to three years prior to the filing of their claims.

The question of whether an employee’s primary duty is the management of an enterprise, department or subdivision, recently supported a decision by the Court of Appeals for the Sixth Circuit that a convenience store manager was an exempt executive.<sup>4</sup> The court first had to consider whether management of the store was Ms. Thomas’ primary duty.

Generally, as determined by the Illinois court in the RadioShack case, the amount of time spent in performance of managerial duties guides whether management is the primary duty of an employee.<sup>5</sup>

Where the employee does not spend the majority of her time in managerial duties, management can still be her primary duty based on the following factors:

1. the relative importance of the managerial duties as compared with other types of duties
2. the frequency with which the employee exercises discretionary powers
3. the employee’s relative freedom from supervision
4. the relationship between her salary and the wages paid other employees for the nonmanagerial work performed by her

In deciding that the Speedway managerial duties were primary, the court relied on the fact that if the store manager failed to perform her managerial duties, her station would not function at all because no one else would perform these essential tasks. Her duties included hiring and assigning staff to work at the store and ordering stock. Therefore, her managerial duties were much more important to Speedway’s success than her non-managerial duties. The court also noted that even though the store manager’s discretion was limited by her district manager’s supervision and Speedway’s standardized operating procedures, she daily exercised discretion over matters vital to the success of her station.

In considering the direction of work criteria of whether a supervisor is an exempt executive, a safety supervisor who had the authority to direct the work of as many as 300 employees on the construction project he supervised was still not exempt, according to the recent decision of a federal trial court.<sup>6</sup> Mr. Jones had authority over employees in the area of safety, and had the power to direct employees how to perform their work in a safe manner. In addition, Mr. Jones could stop the performance of any job that he felt was unsafe, even if the job superintendent disagreed. He could even discipline or discharge an employee who failed to follow his direction in this area. His employer argued that this authority made him exempt from the requirements of the FLSA.

The reviewing court in Florida held that even though Mr. Jones had authority over a large number of employees in the area of safety, he was not an exempt executive. The possibility of disciplining an employee for a safety violation did not mean that he customarily and regularly directed the work of at least 2 employees, as required by the DOL regulations. Directing the work of employees typically includes assignment and direction of work as well as discipline for any appropriate reasons, not just safety violations.

Employers should be sure to review the actual duties of lower level management to determine whether they are exempt from the FLSA as executives. If managerial duties only take up a small amount of time, the manager is only exempt if those duties have particular importance for the employer. Otherwise, that manager may be entitled to overtime under the FLSA.

— END NOTES —

<sup>1</sup>*Corning Glass Works v. Brennan*, 417 U.S. 188, 196-97 (1974).

<sup>2</sup>*Perez v. RadioShack Corp.*, No. 02-884 (N.D. Ill. Nov. 15, 2007).

<sup>3</sup>*Goldman v. RadioShack Corp.*, No 03-0032 (E.D. Pa. 2005).

<sup>4</sup>*Thomas v. Speedway SuperAmerica*, No. 06-3768, 12 WH Cases 2d 1729 (6th Cir. 2007).

<sup>5</sup>29 C.F.R. §541.103 (2003).

<sup>6</sup>*Jones v. Riggs Distiller & Co.*, (M.D. Fla. Dec. 4, 2007). ■

## WILL THE SIXTH CIRCUIT ADOPT A COMMON-SENSE APPROACH TO RETIREE HEALTH CARE?

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For nearly 25 years since the Sixth Circuit's 1983 decision in *UAW v. Yard-Man, Inc.*, 716 F.2d 1476 (6th Cir. 1983), federal trial courts in Michigan and other Sixth Circuit states have routinely held that collectively bargained retiree health care benefits are "vested" under contract language that would be read differently in virtually every other Circuit. A finding of "vesting" means that retiree health care benefits, often negotiated decades ago when health care was far simpler and less expensive, are deemed unalterable, preventing coverage from being discontinued or materially changed. Such a finding may commit the employer-sponsor to future costs for retiree health care that often amount to hundreds of millions of dollars or, in the case of the auto companies, billions of dollars.

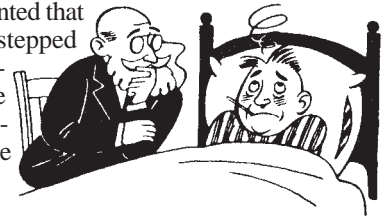
In their zeal to find vesting, courts within the Sixth Circuit have said, for instance, that language merely identifying a pensioner as potentially "eligible" for retiree health care means that the benefit "vested" because this conceptually "ties" the health care benefit to the pension which vests by operation of law when a pension plan's service requirements are met. This rationale has been applied notwithstanding that a pensioner, by definition, would have to be "eligible" for such a benefit in order to have any claim to it – even if that benefit were not vested but terminable.

This state of the law has prompted many employers to attempt to improve the efficiency of their bargained health care plans by introducing modest cost-saving measures – for example, requiring participation in managed health care, instituting reasonable deductibles and co-pays, and mail-ordering common maintenance drugs. So far, such changes typically have come about as a result of negotiations between the union and the employer, sometimes with a court's blessing in a consent judgment.

The Sixth Circuit has yet to address the critical question of whether a so-called vested health care benefit can be modified through the employer's unilateral imposition of sensible plan design changes, some of which were not even available as an option when the underlying obligation was first negotiated. Last fall, in *Prater v. Ohio Education Ass'n*, 505 F.3d 437, 441 (6th Cir. 2007), a Sixth Circuit panel noted that an array of "perplexing questions" remain unanswered in Sixth Circuit law, stating:

What exactly are lifetime healthcare benefits? Does a promise of lifetime benefits mean that they cannot be reduced over the life of a retiree? What if the employer reduces health benefits for active employees or increases the cost of those benefits to active employees? What if the employer increases some health benefits for active employees but reduces others? Must the retiree take the bitter with the sweet? Or is it a ratchet – with only the improvements in health benefits available to the retiree but with no compulsion to take any reduction?

The *Prater* panel commented that these questions could be sidestepped in the case before it, but signaled that they could not be avoided indefinitely. Employers can only hope that the Court will use future opportunities to adopt a common-sense, flexible view of the concept of vesting.



"Are you insured?"

The Seventh Circuit recently adopted just such an approach in a retiree health care case, *Zielinski v. Pabst Brewing Co. Inc.*, 463 F.3d 615 (7th Cir. 2006). Although the underlying benefit was held to have "vested," the Court explained that "[t]he most sensible interpretation" of the agreement creating the right to the benefit would obligate the company to provide prescription-drug benefits at a level "reasonably commensurate" in cost terms to the level originally negotiated. To hold the employer to the literal terms of a plan negotiated in 1974, the court reasoned, "would give the retirees an insanely generous plan relative to today's norms," rather than a plan that would provide them today's cost equivalent. Changes such as keeping the deductible proportional to the cost of the drug and adjusting benefit ceilings in proportion to increasing costs would be permissible as long as the overall benefit remained "reasonably commensurate" to that which was negotiated initially.

The Seventh Circuit thus struck a sensible balance. If retiree health care benefits are to be deemed vested, courts should recognize that the parties did not intend those benefits to be permanently unalterable in the midst of a health care environment that is constantly changing. We hope that when the Sixth Circuit finally addresses these issues, it will recognize that its extraordinarily liberal approach to the vesting issue must at least be balanced by a common-sense rule that allows employers to modernize various features of negotiated retiree health care benefits. ■



### LOOKING FOR *Lawnotes* Contributors!

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For information, contact *Lawnotes* editor Stuart M. Israel or associate editor John G. Adam at Martens, Ice, Klass, Legghio & Israel, P.C., Suite 600, 306 South Washington, Royal Oak, Michigan 48067 or (248) 398-5900 or [israel@martensice.com](mailto:israel@martensice.com).

# MUST EMPLOYERS WORRY ABOUT THE NATIONAL LABOR RELATIONS ACT IF THEIR EMPLOYEES ARE NON-UNION?

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Sure they must, and in more ways than one might think. Most non-union employers recognize that the National Labor Relations Act (NLRA), 29 U.S.C. 151, *et seq.*, applies to them during union organizing activity and the period preceding a union recognition election. To take the most obvious example, an employer cannot discharge an employee for engaging in union organizing efforts, and it may have to answer to the National Labor Relations Board (NLRB) if it does so. Many employers, however, overlook broader application of the NLRA in a non-union setting, particularly with respect to work rules.

Under the NLRA, any work rule prohibiting or likely to have a “chilling effect” on employees’ rights under 29 U.S.C. 157 (Section 7 rights) – the right to engage in union organizing or other concerted activity for mutual aid or protection – may constitute an unfair labor practice. This may be true even for employers who have never seen a union and even if their work rules have never been enforced.

## The Guardsmark Decision

In *Guardsmark, LLC v. NLRB*, 475 F.3d 369 (D.C. Cir. 2007), three relatively common and seemingly innocuous work rules were found to violate the NLRA because of their potential to have a chilling effect on employees’ Section 7 rights, and the employer was ordered to change them.

**Chain-of-Command Rule.** The employer in *Guardsmark*, a security company, had a rule stating generally that employees must follow the “chain of command” in reporting work-related issues. The NLRB challenged a sentence warning: “[D]o not register complaints with any representative of the client.” The NLRB concluded, and the reviewing Court agreed, that this infringed on the employees’ Section 7 rights to solicit sympathy and support from the general public and clients regarding the terms and conditions of employment. The employer’s argument that it did not enforce the rule in a manner that would punish Section 7 activity was rejected; mere maintenance of the rule constituted an unfair labor practice.

**Solicitation and Distribution Rule.** Another *Guardsmark* rule banned “[s]olicitation and distribution of literature not pertaining to officially assigned duties . . . at all times while on duty or in uniform.” The NLRB found that this was also an unfair labor practice, and the Court agreed. In general, employers, whether union or non-union, may prohibit employees from soliciting other employees and distributing literature only during working times and/or in work-

ing areas. Guardsmark’s rule went farther – and crossed the line – by prohibiting an employee from engaging in these protected activities at any time he or she was in uniform, whether the employee was working or not, and whether the employee was in a work area or not.

**No Fraternization Rule.** Yet another Guardsmark rule told employees they must not “fraternize on duty or off duty, date or become overly friendly with the client’s employees or with co-employees.” The NLRB found this rule to pass muster, but the appeals court disagreed. The NLRB concluded that employees would reasonably understand it to prohibit only “personal entanglements,” rather than activity protected by the NLRA. The court ruled, however, that the somewhat vague term “fraternize” could lead employees reasonably to think it prohibited discussions of terms and conditions of employment. The union that filed the charge against Guardsmark argued the word “fraternize” includes having “fraternal” relationships and unions are “fraternal” organizations. It may be best for employers to avoid that word in any “no-dating” or similar policies.

## Confidentiality Rule As Section 7 Violation

In another recent decision, *Cintas Corp. v. NLRB*, 482 F.3d 463 (D.C. Cir. 2007), the D.C. Circuit affirmed an NLRB decision that a confidentiality rule prohibiting employees from disclosing any information about their employment unlawfully restricted the exercise of Section 7 rights. Agreeing with the NLRB, the court held that employees could reasonably construe the rule to restrict discussion of wages and other terms and conditions of employment with co-workers and a union, a reading that chilled their Section 7 rights – even though the company had never enforced the rule in this manner.

## Use of Company E-Mail

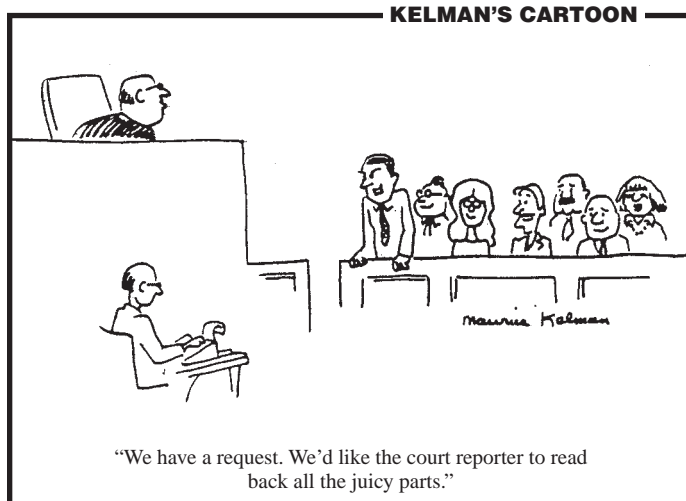
In December 2007 the NLRB issued a much-anticipated decision on whether employees have a statutory right to use an employer’s e-mail system for union communications or other concerted activity. *Guard Publishing Co., d/b/a The Register-Guard*, 351 NLRB 70 (2007), gave a negative answer to that question. An employee who was also the local union president received two written warnings for sending three union-related e-mails in violation of the employer’s written policy, which prohibited use of e-mail to “solicit or proselytize for commercial ventures, religious or political causes, outside organizations, or other non-job-related solicitations.” The NLRB’s General Counsel alleged that the employer violated the Act merely by maintaining the written policy, as well as by issuing the warnings to the employee.

In a 3-2 decision, the Board disagreed. The majority concluded that e-mail use is governed by its precedents dealing with the use of an employer’s equipment. In these decisions, the Board has consistently held that employees have no statutory right to use employer-owned property (including bulletin boards, telephones and televisions) for Section 7 communications, as long as the restrictions are nondiscriminatory. The *Guardsmark* majority adopted a new standard for determining whether restrictions are nondiscriminatory, announcing that “discrimination under the Act means

drawing a distinction along Section 7 lines” and allowing employers to distinguish between personal, nonwork-related postings (such as for-sale notices and wedding announcements) and “group” or “organizational” postings, including union materials. The majority provided a number of illustrative examples of how an employer could draw lines between charitable solicitations and noncharitable solicitations, between solicitations of a personal nature (e.g., an employee offering a car for sale) and solicitations for the commercial sale of a product (e.g., an employee selling Avon products), between invitations for an organization and invitations of a personal nature, etc.

### Right To Co-Worker Representative

In addition to issues relating to work rules, employers need to keep in mind the NLRB’s position on application of so-called *Weingarten* rights for non-union employees. See *NLRB v. J. Weingarten, Inc.*, 420 U.S. 251 (1975). This is the right of an employee, upon request, to have a representative present during an investigatory interview that could lead to the employee’s discipline. (It does not extend to a meeting in which discipline that has already been decided upon is meted out to the employee). Although the Board has flip-flopped several times over the years on the application of *Weingarten* to the non-union workplace, since 2004 the Bush-appointed Board has taken the position that the NLRA does not require a non-union employer to allow a co-worker representative to attend an employee’s investigatory interview. But it remains the Board’s position that a non-union employee may not be disciplined for asking to have a co-worker representative present. And since the politically sensitive Board has reversed itself so many times regarding *Weingarten*’s applicability in a non-union setting, prudent employers should take into account the possibility of this happening again when responding to such a request. ■

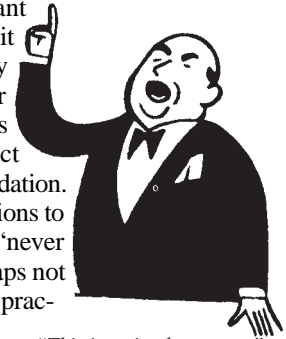


**Editor’s Note:** This Kelman cartoon, and last issue’s, were originally published in *Legal Times* and are reprinted with permission. This cartoon predates the text message era. Any relevance it may bear on current events is purely a tribute to Maury Kelman’s prescience and insight.

## OPENING STATEMENT: TO RESERVE OR NOT TO RESERVE – THAT IS THE QUESTION

**Doug Bonney**  
*Bonney Law Office*

Opening statements serve as the official prologue to any trial or arbitration hearing. And the constant refrain in advocacy training – whether it be trial advocacy or arbitration advocacy – is this: Never waive or reserve your opening statement! The question is whether this advice has any basis in fact or is just received wisdom without foundation. Although there are undoubtedly exceptions to the rule, the evidence suggests that “never waive, never reserve” is valid but perhaps not for the reasons advanced by many trial practice gurus.



“This is a simple case . . .”

In arbitration, you should never waive or reserve your opening, if for no other reason, because arbitrators want to hear your opening immediately. In labor disputes, arbitrators need to hear your opening statements because they usually come into the hearing without any foreknowledge of the dispute and thus need some context for the evidence they are about to receive. See, e.g., Lawrence J. Casazza, “Opening and Closing Statements in Arbitration Advocacy,” *Labor Arbitration: A Practical Guide for Advocates* (BNA Books 1990) at 191; William P. Murphy, “The Ten Commandments for Advocates: How Advocates Can Improve the Labor Arbitration Process,” *Arbitration 1992: Improving Arbitral and Advocacy Skills, Proceedings of the Forty-fifth Annual Meeting, National Academy of Arbitrators* (BNA Books 1993) at 259; Edna E. J. Francis, “What Arbitrators Need from the Parties: Miscellaneous Musings,” *Arbitration 1997: The Next Fifty Years, Proceedings of the Fiftieth Annual Meeting, National Academy of Arbitrators* (BNA Books 1998) at 265.

I have taken that advice to heart and have never reserved my opening. When asked if I wish to make an opening statement in a discharge or discipline case (where the union advocate has the option of reserving), I always answer “absolutely.” I cannot imagine reserving, not because I believe that the arbitrator will automatically decide to rule against my client’s case if I reserve, but because I do not want management’s version of events to go unchallenged for half the hearing. Reserving makes about as much sense to me as deciding not to stomp on the accelerator in a drag race until your opponent is halfway down the straightaway and his tail lights are barely visible.

Despite the uniform drumbeat of advice not to waive or reserve opening statement, I am always surprised when – in a contract or interest arbitration case – a management advocate decides to reserve. And it has happened many times over the years of my experience. I fail to understand what possible tactical advantage the management advocate thinks he will gain by reserving. The only theoretical advantages I have ever read about are that delaying (1) allows the reserving party to hear the opposing side’s entire case before showing its cards, thereby allegedly surprising the opponent

(Continued on page 12)

## OPENING STATEMENT: TO RESERVE OR NOT TO RESERVE – THAT IS THE QUESTION

(Continued from page 11)

by withholding certain facts or defenses and (2) provides continuity between the defense's opening statement and its presentation of evidence, thereby supposedly enhancing the jury's or the judge's understanding of the defense's case. See James W. Jeans, Sr., *Trial Advocacy*, 2d ed. (West 1993) at 10.19, pp. 318-319.

But, in most cases, these supposed tactical advantages are ephemeral. First, a good advocate should be smart enough to anticipate the opponent's facts and theories so as to make the first asserted tactical advantage almost imperceptible in most cases. Second, the jury behavior research shows that delaying opening statement does not provide the hypothetical continuity gain. Surely, the advantage to be gained by having the arbitrator hear both sides of the story overwhelms any slight, theoretical advantage of reserving opening statement.

If you need a reason not to reserve your opening statement other than "arbitrators say so," I can tell you this: The psychological research into jury behavior – to the extent it can be applied to arbitrator behavior – supports the consistent advice not to reserve opening statement. But, contrary to a popular legend, there is no evidence that jurors – or arbitrators – firmly make up their minds based on opening statements alone. Instead, the research shows that jurors start making up their minds during opening statements, and that research provides a scientific basis for not keeping your powder dry.

A statistic commonly bandied about in this debate is that "after hearing opening statements, 65 to 80 percent of jurors . . . make up their minds about the case[.]" Charles Becton & Terri Stein, "Opening Statement," 20 *TRIAL LAWYERS Q.* 10 (Winter 1990). Similar statistics have been passed along from one trial practice luminary to the next for years. See, e.g., Jeans, at 10.2, p. 305 ("It has been discovered that jurors, interviewed after verdict, have confirmed that their ultimate decision corresponded with their tentative opinion after opening statements in over 80% of the cases"). But these authors never provide any citation to the underlying empirical studies, and in fact these statistics appear to be completely apocryphal. William L. Burke, Ronald L. Poulson, & Michael J. Brondino, "Fact or Fiction: The Effect of the Opening Statement," 18 *J. OF CONTEMP. L.* 195 (1992). Contrary to some assertions, the Chicago Jury Project never studied the effect of opening statements. Instead, that research found that "the real decision is reached before deliberation begins" and that most verdicts accord with the majority's tentative initial decisions. Harry Kalven & Hans Zeisel, *THE AMERICAN JURY* at 488-89 (1966). That is a far cry from the claim that most jurors have made up their minds after opening statements.

Although the psychological research on jury behavior may not support a hard and fast statistic like the 80% figure commonly cited in the trial practice literature, the research still provides strong support for the view of arbitrators that you should not reserve your opening statement. One of the first modern studies of the effect of opening statement on juror behavior concluded that the first strong opening statement jurors hear will have the most profound effect on the jurors. T. Pyszczynski & L. Wrightsman, "The Effects of Opening Statements on Mock Jurors' Verdicts in a Simulated Criminal Trial," 11 *J. OF APPLIED SOCIAL PSYCHOLOGY* 301, 309

(1981). The authors of that study theorized that a strong opening statement provides jurors with a thematic framework for interpreting the evidence heard at trial, thus predisposing the jurors to view evidence in a certain way. The authors further suggested that "it may be advantageous for [attorneys] to present opening statements that clearly spell out what the evidence will be and how it should be interpreted." *Id.* at 311-312. This study suggests that it is foolish for an advocate to give a weak initial opening statement. It is a blown opportunity. Moreover, when that happens, this study suggests that the side with the second opportunity at opening should strike with a powerful and complete view of the facts because juror interpretations of equally balanced evidence may be biased toward the side that presents the stronger opening.

The findings of a subsequent study "clearly indicate[d] that the timing of a defense attorney's opening statements can influence perceptions of various aspects of the case." G. Wells, P. Miene, & L. Wrightsman, "The Timing of the Defense Opening Statements: Don't Wait Until the Evidence is In," 15 *J. OF APPLIED SOCIAL PSYCHOLOGY* 758, 769 (1985). That study showed that "delaying the defense opening statement was disadvantageous to the defense" but also showed that the content – strong versus weak – may be unimportant, thus contradicting the results of the earlier study. This article on timing effects also discusses the issues of primacy and recency effects and suggests that further research on those issues is needed.

The bottom line is, however, that delay in making an opening statement is a missed opportunity. The authors of these studies theorized that giving an opening statement at the earliest opportunity is advantageous because it shows the jurors that there are two sides to the story. In the psychological jargon, giving the earliest possible opening primes "a general schema of innocence in the minds of the jurors" while failing to give an opening statement at the earliest opportunity allows the prosecution to imprint its schema indelibly on the jurors' minds. *Id.* at 769-770. We should not allow our opponents to imprint their schema on our arbitrators' or jurors' minds.

Another study showed that promising more than the actual evidence can show can be beneficial. T. Pyszczynski, J. Greenberg, D. Mack, & L. Wrightsman, "Opening Statements: The Effects of Promising More than the Evidence Can Show," 11 *J. OF APPLIED SOCIAL PSYCHOLOGY* 434-444 (1981). This suggests that efforts to put your side's spin on the evidence can work as long as they are not too outlandish and over-the-top. I have often seen good management lawyers do this to beneficial – though irritating – effect. So, we should respond in kind.

This research can help guide us in our advocacy. For example, assume – as is often the case – that the opposing attorney hastily recites the facts and leaves out critical facts that you are sure to rely on in your case. If you reserve your opening statement, the arbitrator will probably accept your opponent's incomplete view of the facts while hearing the initial evidence. But if the you immediately give an opening statement that includes *all* of the relevant facts and stresses that your opponent left out some critical facts, the arbitrator may well view the other side's case with skepticism and give greater credence to your more complete and honest opening statement. At least this is the theory supported by the research, and it mirrors common sense. If you do a better job on your opening statement, you should establish more credibility with the arbitrator and thus enhance your chances of getting a good result for your client. ■

# WHAT NEGOTIATORS OUGHT TO KNOW ABOUT WHY PEOPLE DO WHAT THEY DO – A REVIEW OF *THE SCIENCE OF SETTLEMENT – IDEAS FOR NEGOTIATORS*

Stuart M. Israel

*Martens, Ice, Klass, Legghio & Israel, P.C.*

I was there when Barry Goldman, M.A., J.D., led a sophisticated roomful of lawyers, mediators, and arbitrators in a negotiation for the sale of imaginary sweatshirts.

These weren't just any imaginary sweatshirts. They were high-quality, union-made, hooded, 90% cotton (10% artificial fibers to prevent shrinkage), made-in-the-U.S.A. imaginary sweatshirts. Come to think of it, only imaginary sweatshirts are still made in the U.S.A.

Anyway, this negotiation took place at The Institute of Continuing Legal Education's 2008 Advanced Negotiation and Dispute Resolution Institute. Barry told those on one side of the room that they were the beneficiaries of his largesse. Each would have the gift of the imaginary sweatshirt in the imaginary plastic bag imaginarily sitting on the real table in front of each of them. Unfortunately, Barry advised, he had run out of imaginary sweatshirts. Those on the other side of the room would receive no imaginary gift.

I was on the wrong side. I was disappointed. I like hooded sweatshirts and, in particular, I like free stuff. Too bad Barry hadn't planned better and brought imaginary sweatshirts for everyone.

But, wait, Barry said, there may be a way – through negotiation – to improve the position of all in the room. After all, negotiation is Barry's business. Barry is a lawyer, mediator, and arbitrator, and teaches negotiation at Wayne State University Law School. This is good, because if he was in the imaginary sweatshirt business he couldn't make a living.

So, Barry continued, there likely are those on the one side of the room who would rather have imaginary money than an imaginary sweatshirt and there likely are those on the other side who'd be willing to buy one of the imaginary sweatshirts. Willing sellers and willing buyers. Let's negotiate.

Barry had the sellers write their selling prices on pieces of paper. He had the buyers write their offers on pieces of paper. Barry collected the papers at the front of the room and read the prices and offers aloud. As Barry knew would be the case from past experiments, almost all the selling prices were higher — considerably higher — than most of the offers.

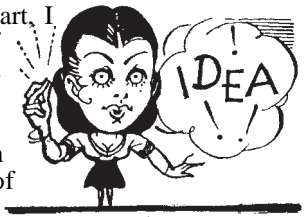
This always happens, Barry told us. It is the product of a psychological influence called the "endowment effect." Human beings "tend to overvalue anything perceived as 'mine.'" So powerful is the endowment effect that it affects the valuation of *imaginary* sweatshirts. Barry explains this in his new book, *The Science of Settlement – Ideas for Negotiators* (ALI-ABA 2008):

People who received an imaginary sweatshirt demanded, on average, twice the amount of money to sell it than those who did not get one were willing to pay. They had become attached to an imaginary object they had pretended to own for two minutes.

I saw the point. I wasn't prepared to part with much imaginary money to buy an imaginary sweatshirt. I've got a drawer full of imaginary sweatshirts at home. But when I donate some of my

imaginary sweatshirts to Purple Heart, I value them quite highly on my list of imaginary charitable deductions. (Note to the IRS: only kidding).

Why does the endowment effect so reliably influence negotiations, both imaginary and real? This is one of many questions answered in *The Science of Settlement*. The endowment effect is one of myriad deep-rooted psychological influences that affect human behavior. These influences are grounded not in the cortex, the rational part of the brain, but in the limbic system, "the evolutionarily older, more primitive emotional part of the brain," formed among the earliest humans, probably in the Pleistocene era. Barry elaborates:



In the ancestral environment it was likely an adaptive strategy to care deeply about your stuff and resist forcefully anyone who wanted to take it from you. Given a population that cared deeply about its stuff and another population that was more blasé, the blasé folks likely did not survive long enough to reproduce and become our ancestors.

Of course, "our evolutionary ancestors are not the ones negotiating the settlement of our lawsuits." Still, Barry writes, "the endowment effect causes people to put undue value on things that belong to them" and "accounts for some of the value your opponent puts on his case, and it accounts for some of the value you put on yours."

The endowment effect may be behind your opponent's assertion that your settlement offer is an "insult." If an offer is taken as an "insult," there is something more at work than a dollars-and-cents cost-benefit analysis. Your opponent's limbic system is telling him that your lowball number disrespects something that "belongs" to him. So, your offer is not merely unacceptable, it is "insulting." As Barry puts it: "The reaction that says 'Screw you and your crummy offer' is an important part of what makes us human."

Being human is what *The Science of Settlement* is all about. Barry explains the psychological influences that affect negotiators and negotiations and tells us how to recognize those influences in action and how to deal with them productively. The "science" referred to in the book title is the considerable body of psychological and neuroeconomic research that Barry makes understandable, useful, and, dare I say, fun for reader-negotiators.

The science tells us, Barry reveals, that the assumption that people act in their rational self-interest – the *homo economicus* model, that the "economic man will always act to maximize his individual economic benefit" – just ain't so. Barry quotes researchers Douglas Yarn and Gregory Todd Jones: "As behavioral negotiation theory has begun to mature, *homo economicus* has begun to evolve into *homo sapiens*."

The science teaches us, and Barry demonstrates throughout *The Science of Settlement*, that many difficulties we encounter in negotiations, with the other side and on our own side, have their roots deep in our brains, driven by unconscious influences and cognitive shortcuts – heuristics – developed by our cave-dwelling ancestors, turned into automatic reactions that may not always be productive in the new millennium. This is stuff that every negotiator will find useful, illuminating why people do what they do, both them and us. Barry observes: "A negotiator who proceeds as though it's all about the money is missing an important feature of human judgment" and "is not doing himself or his clients any favors." You can do a favor for yourself and your clients by reading Barry's book.

The endowment effect and the sweatshirt experiment represent only one of the many, many psychological influences addressed in the book. Some of Barry's section headings provide a glimpse into the book, drawing the reader in to learn more. For example: monkey justice, the Lake Woebegeon effect, base rates, overconfidence, self-serving bias, illusion of control, belief in a just world,

(Continued on page 14)

## WHAT NEGOTIATORS OUGHT TO KNOW ABOUT WHY PEOPLE DO WHAT THEY DO – A REVIEW OF *THE SCIENCE OF SETTLEMENT – IDEAS FOR NEGOTIATORS*

(Continued from page 13)

fundamental attribution error, availability heuristic, probability, the conjunction fallacy, status quo bias, regret aversion, the contrast effect, the similarity-attraction effect, being observed to be listening, anchoring, the winner's curse, reciprocity, rejection then retreat, packaging effects, framing effects, sunk costs, social proof, timing effects, position effects, counterfactuals, the peak-end rule, post-settlement settlement, the lawsuit market, etc., etc.

You've got to read the book to find out what all this means, but here is one example of the "framing effect." Those physicians in a study told that there was a mortality rate of seven percent within five years for a certain operation were hesitant to recommend that operation to patients. On the other hand, those physicians told that there was a 93% survival rate within five years of the operation were more inclined to recommend it to their patients. Of course,



"Hmm, science settles cases."

we lawyers — more intelligent than physicians — understand that the seven percent mortality rate is the same as the 93% survival rate. The study proves the point: framing matters. The way an offer is presented, numbers aside, may trigger a psychological response that is the perception difference between a palatable settlement offer and an "insult."

Barry explores these psychological influences and relates them to negotiation and mediation. In doing so, Barry provides scientific support for some of what is conventional wisdom among negotiators, adding depth to our understanding of why people do what they do. He also debunks some of what is conventional wisdom among negotiators, adding depth to our understanding about why we might want to stop doing what we've been doing. Barry's approach, too, is an antidote to some of the psychobabble that is offered as wisdom by some purporting to educate negotiators.

Barry's book is practical, accessible and readable, and unique. It also is fun and funny. It will help you become a better negotiator. It will provide you with a wealth of information about interesting things that will improve your status as a cocktail party *raconteur* and insightful observer of human nature. There's not much more you can ask from a book.

I need to make a disclosure. I am the editor of *Labor and Employment Lawnotes*, the quarterly published by the State Bar of Michigan Labor and Employment Law Section. Barry writes a regular *Lawnotes* column called "For What It's Worth." He writes about arbitration and mediation and other topics of interest to lawyers and mediators and arbitrators and judges. I find his column, like his book, useful and insightful, and quite amusing. I like Barry's column so much that I encouraged him to write his book. He kindly acknowledges my role in making him a star in the aptly-titled "acknowledgments" section of his book. Still, Barry refuses to share his (admittedly paltry) royalties with me. I am not too exercised about Barry's selfish need to hold on to what he perceives as "his" royalties, because now I understand that it is a product of the endowment effect. On this issue, at least, Barry is stuck in the Pleistocene era.

*The Science of Settlement—Ideas for Negotiators* is available from Barry Goldman ([bagman@ameritech.com](mailto:bagman@ameritech.com)) or from his publisher, American Law Institute-American Bar Association ([www.ali-aba.org](http://www.ali-aba.org)), where one can read the introduction and "preview" chapters. Good reading. ■

## NLRB FRUSTRATIONS

Joseph Marutiak

Service Representative, OPEIU Local 459

It takes a unique person to work for the National Labor Relations Board these days. They used to need people who were familiar with the law, like attorneys. These days they may be better off hiring people who don't mind seeing their work destroyed, like Tibetan monks.

The National Labor Relations Act protects private sector employees' right to organize. The NLRB is supposed to enforce those rights. It is supposed to be both prosecutor and judiciary when it comes to labor law. It receives charges from unions and employees and, similar to the police and prosecutors, investigates and decides whether or not there is reasonable cause to believe the law has been violated. If it has reason to believe the law has not been followed, the NLRB is supposed to convene a trial, provide the charging party with due process and a "day in court" and determine guilt or innocence of the charged party on the evidence. But this no longer happens.

The NLRB still investigates charges. It has hallways full of attorneys who go over charges, take affidavits and research cases. They build a file like the charge was going to court, like it mattered. Then everything stops. When the investigation is done, the NLRB will then look for the best possible reason to defer or dismiss the charge. Either way, the charge becomes irrelevant and the law is not enforced. It reminds one of the works of Tibetan monks.

These monks build elaborate paintings of sand. They spend days on their knees slowly making beautiful sand mandalas. After all that work, they stand up and blow the sand away. For these monks, the destruction of their intricate work is meant to show that our physical life is temporary and not truly real. The monk then goes to work on the next mandala.

NLRB agents have a similar approach. They spend days taking affidavits, interviewing witnesses and building a case. They drag employees to downtown Detroit or Grand Rapids, make them swear an oath and take down every word they say in precise detail. Then, when the investigation is completed, like the monks, they blow it all away. While the monks use wind to destroy their work, the NLRB uses the tools of deferral or dismissal. They are just as effective. They show unions and employees that their complaints are temporary and not real. The agent then begins work on the next file.

While the monks volunteer for their role in the creation and destruction of complex works, employees in the private sector have no choice. The NLRB is the only place to go to try to enforce the NLRA. Employees are like the grains of sand in this analogy. They get blown away. With the NLRB abdicating its role, the law is not enforced. Unfortunately many employers know this and act accordingly. They are like the wind in this analogy, uncaring and unrestrained.

# UNITED STATES SUPREME COURT UPDATE

Regan K. Dahle and Mark W. Jane  
*Butzel Long, P.C.*

The U.S. Supreme Court issued four employment decisions within the span of one week in late February. The cases involved a wide range of issues: from the preemptive reach of the Federal Arbitration Act (“FAA”), to the ability of an individual 401(k) account holder to bring a suit under the Employee Retirement Income Security Act of 1974 (“ERISA”) on behalf of the entire plan. The Court also addressed two questions under the Age Discrimination in Employment of 1967 (“ADEA”): one pertaining to the admissibility of “me-too” testimony, and the other pertaining to the definition of a “charge” for purposes of triggering the 60-day stay on lawsuits.

On February 20, 2008, the Court issued its opinion in *Preston v. Ferrer*, U.S. No. 06-1463. The issue in that case was whether the FAA supersedes state statutes that refer state-law controversies to administrative agencies. In *Preston*, Alex Ferrer, better known as television’s “Judge Alex”, entered into a contract with Arnold Preston, an entertainment attorney. In June 2005, Preston sought fees allegedly due under the contract and invoked the contract’s arbitration provision, which stated that the parties agreed to arbitrate “any dispute...relating to the terms of [the contract] or the breach, validity, or legality thereof...in accordance with the rules [of the American Arbitration Association].” Ferrer countered a month later that the contract was invalid and unenforceable under California’s Talent Agency Act (“TAA”) on the grounds that Preston acted as a talent agent without the requisite license, thereby rendering the entire contract void. The TAA vested jurisdiction over such disputes in the California Labor Commissioner. This created a controversy over which entity, the arbitrator or the Labor Commissioner, had authority to decide whether Preston acted as a talent agent.

Ferrer filed suit in state court seeking to enjoin the arbitration. He received a favorable decision from the California Court of Appeals that *Buckeye Check Cashing, Inc. v. Cardegna*, 546 US 440 (2006) (which held that challenges to the validity of a contract providing for arbitration should be considered by an arbitrator, not a court) was inapposite on the grounds that *Buckeye* did not involve an issue in which an administrative agency had exclusive jurisdiction over a dispute. The U.S. Supreme Court disagreed, holding that when parties agree to arbitrate all questions arising under a contract, state statutes which place primary jurisdiction in another forum, whether the forum is judicial or administrative, are superseded by the FAA. The Court reasoned that Ferrer was, in effect, seeking to invalidate the contract as a whole, rather than merely attempting to challenge the validity of the arbitration clause. Such attempts to invalidate an entire contract, when the contract specifically provides that the parties have agreed to arbitrate disputes between them, will fail due to the well-established rule that the FAA displaces conflicting state law. The Court did not believe that an administrative agency that had been vested jurisdiction by a state statute was any different than a judicial entity, because the mere

involvement by an administrative agency in the enforcement of a statute does not limit private parties’ obligations to comply with their arbitration agreement.

Also on February 20, 2008, the Court issued its opinion in *LaRue v. DeWolff, Boberg & Assoc., Inc.*, U.S. No. 06-856. LaRue sued his former employer, DeWolff, and the retirement plan administered by DeWolff (the “Plan”). The Plan was a 401(k) plan that allowed participants to direct the investment of their individual account balances. LaRue alleged that he directed DeWolff to make certain changes to his investments, but DeWolff failed to do so. LaRue claimed that this failure was a breach of fiduciary duty that caused his account to lose approximately \$150,000. Initially, LaRue sued under §502(a)(3) of the Employee Retirement Income Security Act of 1974 (“ERISA”), but his claim was dismissed because §502(a)(3) only permits suits in equity. LaRue appealed the dismissal, asserting that his claim could also be pursued under §502(a)(2), because that subsection permits suits to be brought on behalf of the plan against fiduciaries who have breached their fiduciary duties under ERISA. The Fourth Circuit Court of Appeals affirmed the lower court’s decision that LaRue could not bring suit under §502(a)(3) and also held that *Massachusetts Mutual Life Ins. Co. v. Russell*, 473 US 134 (1985) limited the availability of a suit under §502(a)(2) to those instances where the claim was brought on behalf of the plan for the benefit of the entire plan, rather than to recover a loss to one participant.

The U.S. Supreme Court ruled in favor of LaRue, holding that while §502(a)(2) does not provide a remedy for individual injuries that are separate and distinct from the plan, it does authorize recovery for fiduciary breaches that impair the value of plan assets in a participant’s individual account. The Court noted that since its prior decision in *Russell*, defined contribution plans with individual accounts have become far more prevalent. Where individual accounts are maintained, a fiduciary breach may diminish the assets of a single participant without affecting the entire plan. The Court also commented that ERISA §404(c), which protects fiduciaries from liability for losses caused by the participants’ exercise of control over the assets in their individual accounts, “would serve no real purpose if...fiduciaries never had any liability for losses in an individual account.”

On February 26, 2008, the Court issued its opinion in *Sprint/United Management Co. v. Mendelsohn*, U.S. No. 06-1221. Sprint terminated Mendelsohn in 2002 as part of an ongoing company-wide reduction in force. Mendelsohn sued under the ADEA alleging disparate treatment based on her age. Mendelsohn sought to introduce the testimony of five other former Sprint employees who claimed that their supervisors discriminated against them because of age. None of the employees worked in Mendelsohn’s division, nor had any of them worked under, or heard any discriminatory remarks by, the supervisors in Mendelsohn’s chain of command. Sprint filed a motion in limine to exclude this testimony about discrimination against employees “not similarly situated” to Mendelsohn, which the trial court granted without providing any analysis as to the specific facts of the case. The Tenth Circuit reversed the trial court, holding that the motion in limine should have been denied. The U.S. Supreme Court reversed the Tenth Circuit. The Court noted that appellate courts afford broad

(Continued on page 16)

## UNITED STATES SUPREME COURT UPDATE

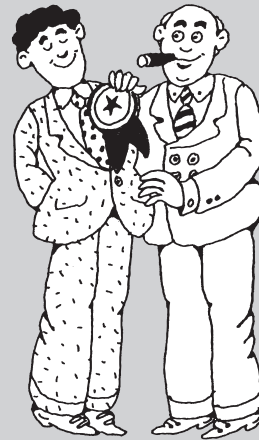
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deference to a trial court's evidentiary rulings due to the trial court's familiarity with the details of the case, and its experience in handling evidentiary matters. The Court reasoned that the trial court's order failed to give any analysis as to why the evidence lacked sufficient probative value or was unduly prejudicial. As a result, the Court held that the Tenth Circuit should have remanded the case to the lower court for clarification rather than assess the probative value and potential prejudicial effect of the evidence itself. The Court concluded that the issue of whether evidence of discrimination by other supervisors is relevant in an individual ADEA case is fact-based and context-specific. As a result, because Federal Rules of Evidence 401 and 403 do not make such evidence per se admissible or per se inadmissible, such inquiry belongs to the trial court in the first instance.

Finally, the Court issued its opinion in *Federal Express v. Holowecki*, U.S. No. 06-1322 on February 27, 2008. In *Holowecki*, the plaintiffs consisted of 14 current and former Federal Express ("FedEx") couriers over the age of 40 who alleged that FedEx's programs which tied courier compensation and continued employment to performance benchmarks (i.e. the number of stops a courier makes per day) violate the ADEA. The plaintiffs contended that the programs were veiled attempts to force out older workers before they were entitled to retirement benefits. FedEx moved to dismiss the suit of one of the plaintiffs, Patricia Kennedy, on the grounds that she had failed to file her charge with the EEOC at least 60 days prior to filing suit. Kennedy contended she submitted EEOC Form 283 (an "Intake Questionnaire"), along with a signed affidavit describing in greater detail the alleged discriminatory employment practices, more than 60 days prior to entering the suit. The affidavit asked the EEOC to force FedEx to end its discriminatory plan. The lower court dismissed the case on the grounds that the documents Kennedy filed were not a "charge," a decision later reversed by the Second Circuit Court of Appeals. FedEx appealed to the U.S. Supreme Court.

The Court considered what constitutes a "charge" under the ADEA. Particularly, the Court reviewed the language of ADEA §626(d), which provides that an individual may not sue for 60 days after bringing a charge alleging unlawful discrimination with the ADEA, and that once an individual brings a charge, the EEOC must promptly notify all persons named in the charge and attempt to informally eliminate any alleged unlawful practices. The Court held that a charge must be reasonably construed as a request for the agency to take remedial action. The Court nevertheless cautioned that the ruling does not require the EEOC to actually take action in order for an individual's filing to constitute a charge. As a result, even though the EEOC failed to treat Kennedy's Intake Questionnaire as a charge (and thus failed to notify FedEx about Kennedy's potential claim prior to suit), due to the fact that the affidavit attached to the Intake Questionnaire requested the EEOC to force FedEx to stop its practices, Kennedy had sufficiently brought a "charge" and waited the requisite 60 days. ■

## LABOR AND EMPLOYMENT LAW SECTION



### DISTINGUISHED SERVICE AWARD NOMINATIONS

The Council of the State Bar of Michigan Labor and Employment Law Section is seeking nominations for the Section's Distinguished Service Award.

The Section presents its Distinguished Service Award to recognize individuals who have made outstanding contributions to the practice of labor and/or employment law. Award recipients are recognized at the Section's mid-winter meetings in January. Each recipient may designate a \$1,000 scholarship at a Michigan law school.

The Award is presented to individuals who:

1. Have made major contributions to the practice of labor and/or employment law;
2. Reflect the highest ethical principles;
3. Have advanced the development of labor and/or employment law;
4. Have a long-established commitment to excellence; and
5. Are recognized and respected by all constituencies in the Section.

Past recipients include Ted Sachs, Bill Saxton, Ted St. Antoine, George Roumell, Erwin Ellmann, Jim Tobin, Joe Marshall, John Brady, Gordon Gregory, Carl VerBeek, Bob Battista, Rhett Pinsky and Leonard Page.

Nominations may be submitted to LELS Distinguished Service Award c/o Timothy H. Howlett at Dickinson Wright PLLC, 500 Woodward Avenue, Suite 4000, Detroit, MI 48226, fax: (313) 223-3598, e-mail: [thowlett@dickinsonwright.com](mailto:thowlett@dickinsonwright.com), or c/o Megan P. Norris at Miller Canfield Paddock & Stone PLC, 150 W. Jefferson, Suite 2500, Detroit, MI 48226, fax: (313) 496-8453, e-mail: [norris@millercanfield.com](mailto:norris@millercanfield.com).

Please address the five award criteria when you submit a nomination. Nominations for 2008 consideration must be received by November 1, 2008.



## FOR WHAT IT'S WORTH

**Barry Goldman**  
*Arbitrator and Mediator*

*Woe unto you also, ye lawyers! For ye lade men with burdens grievous to be borne . . .* Luke 11:46

I applied for a job not long ago. A colleague asked if I would teach a course at a local community college. It was one of those quickie courses that meet over three Saturdays. I taught the class and submitted the grades, and then the nice people at the college told me there were certain forms I had to fill out before I could get paid. They sent me a packet of 22 items:

1. New Hire List
2. Welcome
3. Application for Employment
4. I-9 Form
5. Federal Withholding Form, W-4
6. State Withholding Form MIW-4
7. Beneficiary Form
8. Employee Office Data Sheet
9. Right-To-Know
10. Drug Free Workplace Memo and Pamphlet
11. Sexual-Harassment Memo and Fact Sheet
12. Computer Software Piracy
13. Prevention of Workplace Violence Policy
14. Direct Deposit Form
15. Voluntary Options: 403(b) and 457 Income Deferrals
16. Comparison of 403(b) and 457 Retirement Plan
17. Verification of Work Experience
18. Application For Approval to Teach Vocational-Technical Post Secondary Courses
19. OATH
20. MEA Union Membership Application
21. Adjunct Faculty Paperwork Checklist
22. Detroit City Withholding Form

All my contact with students was over. There was no longer any possibility of my sexually harassing anyone or committing acts of violence against them. All danger of my selling illegal drugs to my students had passed. If I was an illegal alien, it was too late to prevent me from polluting the campus with my presence. If I was going to infect my students with seditious propaganda, I had already done so. In other words, few of the forms in the packet had any actual meaning.

But processing my application took several weeks.

Why? Partly because of politicians and bureaucrats. The fact that a piece of legislation doesn't make any *sense* is not a deterrent to a politician. If a liberal legislator believes there is a problem with dangerous chemicals in the workplace, he is likely to propose a law requiring that employees be so informed. Passing such a law gives the appearance of having done something about the problem. If a conservative politician believes there is a problem with Communist college professors preaching the violent overthrow of the government, he is likely to propose a law requiring a (notarized) loyalty oath for the same reason.

Pointlessness is also not a deterrent to a bureaucrat. If you tell a bureaucrat he must have a signature on the Dangerous Chemicals in the Work Place form before he can process a paycheck, the fact there are *are* no dangerous chemicals in a college classroom doesn't phase him.

It is certainly true, to paraphrase Diderot, that mankind will never be free until the last politician is strangled with the entrails of the last bureaucrat.

But responsibility does not rest with politicians and bureaucrats alone. Part of the problem lies with lawyers. When greedy and cynical plaintiff's lawyers file meritless lawsuits, fearful and stupid defense lawyers give their clients bad advice. And vice versa. This is "the rule of lawyers not of men" and it is the cause of much that is grievous to be borne.

Look, some of my best friends are lawyers. But lawyers make legaldygook like squid made ink. And when cynical politicians and stupid bureaucrats have legal cover for their depredations there is no limit to the suffering they can impose. And they can say "The lawyers made me do it."

# GVSU AND MSU WEB SITES FOR PUBLIC SECTOR LABOR LAW

Maris Stella (Star) Swift

Grand Valley State University has a free web site that was developed primarily for its students studying collective bargaining and labor law but the site is open to the public and many labor lawyers and arbitrators have already found it helpful. The site has numerous public sector grievance arbitration awards that were contributed by arbitrators, attorneys, public sector unions and employers. The awards are catalogued and summarized by the arbitrator's name and by the issue(s) in the case. The names of the parties in the award have been deleted or changed. Awards are identified by the last name of the arbitrator (Smith #1, Smith #2, etc.). Over the past year the web site has had an average of 3,000 hits per month but when we recently linked the site to Wikipedia our numbers jumped up to 6,000 hits per month.



The site has a list of all MERC arbitrators and fact finders and a resume for each neutral. The web site also has numerous links that are relevant to the public sector labor practice. If you would like to look at the site go to: <http://www.gvsu.edu/arbitrations/>

If you would like to contribute any public sector grievance awards to the site please send them to me as a Word attachment at: [swifts@gvsu.edu](mailto:swifts@gvsu.edu)

Michigan State University also has a free web site that many of you already use to find fact finding and Act 312 awards. In addition, the site now contains several public sector collective bargaining agreements. There are many old and new collective bargaining agreements and the contracts are linked to related fact finding and 312 awards. The site also provides pertinent information about cities, counties and townships that will be useful in collective bargaining. The web site has an average of 3,000 hits per month.

The Labor and Employment Section has provided funding for this web site for the past two years. The site would not be possible without the Section's donations. You may view the MSU web site at: <http://www.lib.msu.edu/coll/main/lir/>

If you would like to contribute current public sector labor contracts to this site please send them to the Michigan State's Head LIR librarian, Laura Leavitt at: [Leavitt9@msu.edu](mailto:Leavitt9@msu.edu) Laura is an excellent resource librarian and is happy to help you learn how to navigate her web site or find a needed document. You should feel

very comfortable sending her an e-mail with your questions. My experience with Laura is that she is always timely in her responses and she often offers more resources and ideas than I ever thought possible.

Current arbitration awards and labor contracts are wonderful teaching tools for our students. Grand Valley State University and Michigan State University hope that you will consider taking the time to e-mail us your awards and contracts. There is no better way for our students to understand labor relations than through arbitration awards and collective bargaining agreements.

At GVSU we have our fourth year under graduate students in our Grievance Arbitration and Collective Bargaining class divide into teams for the semester (union and employer). First they conduct investigatory interviews, decide on discipline, manage their way through the grievance chain and then eventually try their arbitrations before attorneys and arbitrators. During the second half of the semester each team negotiates a complete collective bargaining agreement. Every student in the class says that while it is a very time consuming course, the practical use of arbitration awards and labor contracts helps them truly understand the process and the law. Several of my former students contact me and say that their employers cannot afford to pay for a fee based web site so the GVSU-MSU web sites are a valuable resource for them too. I hear the same comments from arbitrators, unions and employers on a regular basis.

This summer we have a grant to add more public sector grievance arbitration awards to our GVSU web site. We will use students to remove all the identifying information, summarize the awards and catalogue the awards. It saves us time if you send us the awards by e-mail in a Word format but if you



only have a paper copy we are happy to take them too. I personally will read the awards to be sure that all identifiers have been removed after the students have worked on them. You also have the option of reading the awards (post deletions) before they are placed on our web site for public viewing or deleting the information yourself before you send us the awards. If you have paper copies of grievance awards that need to be scanned please send them to me at the following address: Prof. Maris Stella Swift, 448C DeVos Center, Grand Valley State University, Grand Rapids, Michigan 49504-6431 Also please feel free to call me if you have any questions at: 616-331-7453. ■

## LEL LINKS

**Kathryn VanDagens**

The GVSU and MSU websites described in Star Swift's article are only two of many websites now bookmarked especially for our members on the LELS section of the State Bar website, [michbar.org](http://michbar.org). Now, after opening "Links of Interest" on the LELS section web page, with just a few clicks of your mouse you can research the DOL regulations regarding the Family Medical Leave Act, the proceedings of the National Academy of Arbitrators, or one of many other practice-related websites. The links have been selected with LELS practice areas in mind, so we hope you find this addition to our website useful. If you have suggestions for additions, please let me know at [kvandagens@comcast.net](mailto:kvandagens@comcast.net).

### Michigan Law & Governmental Agencies

Michigan Legislature

[www.legislature.mi.gov](http://www.legislature.mi.gov)

Michigan Department of Civil Rights

<http://www.michigan.gov/mdcr>

Michigan Department of Labor and Economic Growth

<http://www.michigan.gov/dleg>

Michigan Employment Relations Commission (MERC)

[http://www.michigan.gov/dleg/0,1607,7-154-10576\\_17485--,00.html](http://www.michigan.gov/dleg/0,1607,7-154-10576_17485--,00.html)

Collection of Fact Finding Reports and Act 312 (1969)

Arbitration Awards

<http://turf.lib.msu.edu/awards/>

Michigan Grievance Arbitration Awards

<http://www.gvsu.edu/arbitrations/>

Michigan State University's Labor and Industrial Relations Library

<http://www2.lib.msu.edu/branches/lir/index.jsp>

### Federal Courts & Federal Agencies

United States Court of Appeals for the Sixth Circuit

<http://www.ca6.uscourts.gov/internet/index.htm>

United States District Court for the Eastern District of Michigan

<http://www.mied.uscourts.gov/>

United States District Court for the Western District of Michigan

<http://www.miwd.uscourts.gov/>

Federal Mediation and Conciliation Service

<http://www.fmcs.gov/internet/>

National Labor Relations Board

[www.nlr.gov](http://www.nlr.gov)

U.S. Equal Employment Opportunity Commission

[www.eeoc.gov](http://www.eeoc.gov)

U.S. Department of Labor-General

[www.dol.gov](http://www.dol.gov)

U. S. Department of Labor: The Fair Labor Standards Act

<http://www.dol.gov/compliance/laws/comp-flsa.htm>

U. S. Department of Labor: Family Medical Leave Act

<http://www.dol.gov/esa/whd/fmla/>

U. S. Department of Labor: Occupational Safety & Health Administration

<http://www.osha.gov/>

U. S. Department of Labor: Veterans' Employment & Training Service (including USERRA)

<http://www.dol.gov/vets/>

### Associations and Agencies

American Arbitration Association

[www.adr.org](http://www.adr.org)

American Bar Association Labor and Employment Section

<http://www.abanet.org/labor/home.html>

Labor and Employment Relations Association (National)

<http://www.lera.uiuc.edu/>

Labor and Employment Relations Association (Detroit Chapter)

<http://www.emich.edu/lera/>

Labor and Employment Relations Association (Mid-Michigan Chapter)

<http://msu.edu/user/lera/Resources.html>

Dispute Resolution in the Workplace-The Proceedings of the National Academy of Arbitrators

<http://www.naarb.org/proceedings/index.asp> ■

## NATIONAL LABOR RELATIONS BOARD UPDATE

**Stephen M. Glasser**

*Regional Director, Region 7 – Detroit*

An oft-asked question in recent months is: "How is the Board functioning with only two members?" The answer is that it is indeed functioning and issuing decisions. As background, upon the expiration of Chairman Robert Battista's term on December 16, 2007, and in anticipation of the expiration of Members Peter Kirsanow's and Dennis Walsh's terms, on December 28, 2007 the Board (Members Liebman, Schaumber, Kirsanow, and Walsh) delegated its full powers to a three-member group. With the departures of Members Kirsanow and Walsh on December 31, 2007, the Board presently consists of recently named Chairman Schaumber and Member Liebman who constitute a quorum of a three-member group. When they agree as to the disposition of a case, be it a representation or unfair labor practice case, they issue their decision. When they are unable to agree, then no decision issues. And, of course, there will be no overruling of precedent with only two members. In this respect, the board will overrule precedent only with four or five sitting members.

It should be noted that in addition to the Board's delegation of powers noted above, it also delegated to the General Counsel final authority in respect to Section 10(j) (injunction relief) and contempt proceedings.

At the Regional Office level, it is business as usual. Representation and unfair labor practice cases are being processed as if there was a full Board. Those cases that end up before the Board will be treated in accord with Chairman Schaumber's and Member Liebman's views of the case. For now, wherever possible they are trying to reach agreement in as many cases as possible so as to avoid what would otherwise be a growing inventory of undecided cases. Whether the President will nominate and the Senate confirm additional Board members between now and the general elections anyone's guess.



## VIEW FROM THE CHAIR

David B. Calzone, *Chair*  
*Labor and Employment Law Section*

The following is excerpted from the 2007-2008 LEL Section Annual Report to the State Bar of Michigan.

**Mission Statement:** The purposes of the Section shall be to study the law of labor relations and to promote its fair and just administration; to study and report upon proposed and necessary legislation, to promote the legal education of members of the Bar and the general public by generating awareness of the problems and concerns of management, labor, and employment relations through sponsorship of meetings, institutes, and conferences, and by preparing, sponsoring, and publishing legal writing in the labor field; to endeavor to assist in the development of rules of conduct based upon the rights and responsibilities of labor and industry; and to promote justice, human welfare, and industrial peace.

**2007-2008 Council Meetings:** The Council meets once a month, typically on the second Monday of the month, during every month except July and August. During the last year, the meetings were held in Bloomfield Hills, Northville and Okemos.

**Events and/or Seminars:** This has been an active year for the Labor and Employment Law Section.

On September 27, 2007, at the Annual Meeting of the State Bar of Michigan, the Labor and Employment Law Section held its Annual Meeting and conducted an educational seminar consisting of a keynote speech by The Honorable Kurtis T. Wilder from the Michigan Court of Appeals, a panel discussion on the differences between state and federal employment discrimination laws and case law by Mary Anne Helveston and Katherine Smith-Kennedy, and a discussion of e-discovery for employment litigators by James Boutrous.

On October 24, 2007, the Section continued its longstanding tradition of co-sponsoring the Bernard Gottfried Memorial Labor Law Symposium at Wayne State University Law School and purchasing scholarships for law students to attend the Symposium.

On the evening of December 17, 2007, the Section conducted a Holiday Reception at the Townsend Hotel in Birmingham, Michigan. The keynote speaker for this year's Holiday Reception was Michigan State Representative and Majority Floor Leader, Steve Tocobman, who discussed

Michigan's budget crisis. The Holiday Reception was once again organized by former Section Chair, Deborah Gordon. Deb developed the idea for a Holiday Reception several years ago and has organized the event every year since its inception.

The Section's Mid-Winter Meeting was held on January 25-26, 2008 at the Historic Detroit Athletic Club. At the Section Dinner on January 25, the Section honored longtime Detroit labor law attorney and former General Counsel of the National Labor Relations Board, Leonard Page, with its Distinguished Service Award. Leonard's distinguished career was recounted by his longtime friend and colleague, Samuel McKnight. The Dinner also featured an entertaining performance by the Detroit-area musical parody group, A (Habeas) Chorus Line, whose members are primarily Detroit-area lawyers. On January 26, the Section held an educational program consisting of a MERC Update by Jeffrey Donahue, an NLRB Update written by Stephen Glasser and presented by Erikson Karmol, an EEO Update by Jeffrey Steele, a Capitol Hill(s) Update by Robert Boonin, a panel discussion on the continuing violations theory by The Honorable Robert J. Colombo, Jr. of the Wayne County Circuit Court, Lawrence Murphy and Michael Pitt, and a second panel discussion on trying the high-profile employment case by Kathleen Bogas and Deborah Gordon.

On April 10-11, 2008, the Section co-sponsored the Institute for Continuing Legal Education's 33d Annual Labor and Employment Law Institute at St. John's Conference Center in Plymouth, Michigan. The Institute is the largest and most comprehensive labor and employment law educational program held in the State of Michigan each year.

On June 11, 2008, the Section will be holding a "Spring-Board" seminar at The reserve at Big Rock Chop House in Birmingham, Michigan. The event is designed to inform and empower attorneys to excel in their practices and take charge of their careers. The seminar consists of three, 30-minute roundtable discussions that allow participants to talk with facilitators representing the bench, defense and plaintiff attorneys, and the management side of law firms. Topics will include business development for newer attorneys, upward mobility in law firms and alternative works arrangements, and alternative and e-discovery. A two-hour networking and socializing reception with hors d'oeuvres and beverages will follow the roundtables.

**Other Activities:** The Section has adopted an initiative this year to make a concerted effort to attract participation and commitment from newer members of the Section so as to build the foundation that will

carry the Section forward during the next couple of decades. The Council asked a subcommittee consisting primarily of newer members of the Section to help design programs and events that will not only directly involve newer labor and employment lawyers but will also encourage such lawyers to participate actively in future Section events. This subcommittee, which is led by Dan Swanson and Tim Howlett, consists of Anne Marie Welch, Brett Rendeiro, Brian Koncius, Charlotte Carne, Michael Chichester, Eric Pelton, Jay Boger, John Conway, Kevin Carlson, Mike Shoudy, Phyllis Gayden, Randy Barker, Ryan Mulally, Kevin Stoops and Susan Hiser, developed the idea and format for and then organized the "Spring-board" seminar and networking reception to be held on June 11.

The Section is also exploring ways of improving its web page on the State Bar's website and has already made some improvements by adding a Links of Interest Page (thanks to Kathryn Van Dagens), a Membership Directory, back issues of the Section's publication, *Lawnotes*, and selected written materials from educational programs.

The Section also provided financial assistance to the Michigan State University Labor and Industrial Relations Library's project to develop a searchable collection of Act 312 Awards and Fact Finding Reports.

The Section continues to publish its quarterly journal, *Lawnotes*, under the able and creative leadership of Stuart Israel. Stu and his assistant editors, John Adam and Andrew Nickelhoff, continually produce an extremely high quality journal that features thought-provoking articles about cutting edge labor and employment law issues, regular updates from Michigan and local federal courts, and entertaining and frequently humorous musings about the practice of law.

This past year has been a busy and successful one for the Section, due in no small part to a group of extremely hard working, dedicated and forward-thinking Council members, who have enhanced the stature and professionalism of our Section within the State Bar. Without the Council's efforts and the efforts of the many Section members who have volunteered their time and abundant talents to the Section's programs, the various programs and accomplishments discussed in this report would not have happened.

## SUPREME COURT ENLARGES CATEGORY OF DISCRIMINATION CLAIMS SUBJECT TO LIABILITY UNDER 42 U.S.C. §1981

William M. Saxton  
Butzel Long, P.C.

The Civil Rights Act of 1866, 42 U.S.C. § 1981, as initially enacted provided that "all persons [within the jurisdiction of the United States] shall have the same right . . . to make and enforce contracts as is enjoyed by white persons."<sup>1</sup>

In *Patterson v. McLean Credit Union*, 491 U.S. 164 (1989), the Court held that Section 1981 had limited reach and could not be construed as a general proscription of racial discrimination in all aspects of contract relations. The Court ruled that Section 1981 prohibits racial discrimination only in the "making and enforcement" of contracts and said that the right to make and enforce contracts does not extend to conduct by an employer after the contract relationship has been established. Thus, the Court held that a racial harassment claim was not actionable under Section 1981.

In 1991, Congress passed the Civil Rights Act of 1991 which was clearly aimed at superseding the Court's holding in *Patterson v. McLean*. The new law added a new subsection to Section 1981, which says:

Make and enforce contracts defined.

For purposes of this section, the term "make and enforce contracts" includes the making, performance, modification and termination of contracts and the enjoyment of all benefits, privileges, terms and conditions of the contractual relationship. 42 U.S.C. § 1981(b).

In *CBOCS v. Humphries*, \_\_\_ U.S. \_\_\_ (May 27, 2008) respondent claimed that he was discharged in retaliation for his complaining about the dismissal of another black employee. He filed a complaint alleging that CBOCS' action violated both Title VII and Section 1981. The trial court granted CBOCS' motion for summary judgment on Humphries' Section 1981 claims. The Seventh Circuit reversed. The issue presented to the Supreme Court was "whether § 1981 encompasses retaliation claims."

The Court acknowledged that the 1991 amendment to Section 1981 nullified its decision in *Patterson v. McLean*. The Court then concluded that its pre-*Patterson v. McLean* decisions construing 42 U.S.C. § 1982<sup>2</sup> (which prohibits race discrimination in real estate transactions) and principles of *stare decisis* lead to the conclusion that Section 1981 includes claims of racial retaliation.

The *CBOCS* decision has practical implications. Heretofore, Title VII was the sole avenue for pursuing employment-related claims of retaliation under federal law. Title VII requires that a charge of retaliation must be filed within 300 days of the alleged retaliation, a relatively short period of limitation. But, the statute of limitations for Section 1981 claims of retaliation is four years. 28 U.S.C. § 1658.

In a Title VII action the sum of all compensatory and punitive damages awarded is capped at from \$50,000 to \$300,000, depending on the number of employees in the employer's workforce. But, Section 1981 places no limits on the amounts of compensatory and punitive damages that can be awarded to a prevailing plaintiff.

Title VII covers only those employers who have 15 or more employees. Section 1981 applies to all employers regardless of the number of persons they employ.

The Court's decision in *CBOCS v. Humphries* significantly raises the stakes with regard to race-based claims of retaliation.

— END NOTE —

<sup>1</sup>Racial discrimination against whites as well as against non-whites is within the section's coverage. *McDonald v. Santa Fe Trail Transportation*, 427 U.S. 273 (1976).

<sup>2</sup>See *Sullivan v. Little Hunting Park, Inc.*, 396 U.S. 229 (1969). ■

# ACT 312 ARBITRATOR AND FACT-FINDER TRAINING OPEN TO ADVOCATES

Ruthanne Okun, *Bureau Director*

D. Lynn Morison, *Staff Attorney*

*Bureau of Employment Relations, Michigan Department of  
Labor and Economic Growth*

The mission of the Bureau of Employment Relations/Michigan Employment Relations Commission includes fostering peaceful and cooperative employer-employee relations through education and training. We often provide training for our constituents and prepare informative documents in furtherance of this mission. Educational materials are posted on our website at [www.michigan.gov/merc](http://www.michigan.gov/merc), including: past MERC decisions, frequently asked questions about various employment matters and about MERC, and the statutes and rules that we administer. We have also arranged for the printing of a booklet that contains those statutes and rules, as well as the recently revised version of our easy-to-read booklet "Guide to Public Sector Labor Relations in Michigan: Law & Procedure Before the Michigan Employment Relations Commission."

Consistent with the education and training component of our mission, it is our goal to ensure that those on our panels of Act 312 arbitrators and fact finders remain current on changes in the law and bargaining trends that may affect the handling of their assigned cases. On October 31, 2008, we will conduct training for our panel members and invite you to participate in the planning and, possibly, in the training.

As we sketch out details for this upcoming program, we look to you to suggest topics that will benefit our panel members. We believe that you, the advocates who frequently appear before us, are in the best position to suggest subjects for the agenda that will allow us to maximize the limited training time available. Our current plans for the program include an all-day session for those recently added to the panels, and a half-day for those more experienced. Our program will include a legal update, focusing on MERC and court decisions that have implications for Act 312 and fact finding proceedings. We also anticipate including sessions on utilizing and working with MERC mediators to settle cases, expedite proceedings, or to reduce the number of issues before the panel. The program is likely to include a presentation by ALJs from the State Office of Administrative Hearings and Rules (SOAHR) concerning litigating unfair labor practice and/or bargaining unit issues simultaneously with on-going Act 312/ or Fact Finding proceedings. Finally, we expect to include a workshop on the latest trends in providing health care coverage for both active employees and retirees, via Health Savings Accounts (HSAs), Health Retirement Accounts (HRAs), and Voluntary Employee Beneficiary Associations (VEBAs). We look forward to receiving your suggestions for training topics and/or presenters, which you are welcome to send to [okunr@michigan.gov](mailto:okunr@michigan.gov) before August 31, 2008.

With the financial support of Michigan State University College of Law, MERC has scheduled the training session in the beautiful environs of the Inn at St. John's in Plymouth, Michigan on October 31, 2008. We have moved the training to the Inn as a convenience to the majority of our panel members; also, this location will allow us to open up the program to a limited number of advocates and others. If you think you will be interested in attending the training, please pencil the October 31 date on your calendar and, peruse the "What's New?" feature on our web-page from time to time, or call our offices (before September 15) to reserve your place in the audience.

In recent years, we have found that fulfilling the training and education part of our mission to be a challenge, as our training budget has been limited. The impetus for arranging the October program comes from Professor Mary Bedikian, Director of the Alter-

nate Dispute Resolution program at MSU's College of Law. Fortunately, we have found a partner in MSU's law school, and they have graciously provided the financial assistance needed to allow us to further our mission. The upcoming training is the third MERC training program supported by the MSU College of Law. Previous programs were held in 2004 and 2006. We recognize that we are fortunate to receive the law college's continued support during this challenging time and extend our sincere appreciation to Professor Bedikian and to the law school administration.

Finally, both the law school and the Labor and Industrial Relations School at MSU have been most helpful in providing us with sufficient funds to print hard copies of MERC's newly updated version of its "Guide to Public Sector Labor Relations in Michigan." This document is posted on our agency's web-site at [www.michigan.gov/MERC/publications](http://www.michigan.gov/MERC/publications). Hard copies may be purchased for a mere \$5 and are available by contacting our office. ■



## THE JOY OF LABOR LAW

**Congress and *Primum Non Nocere*.** It would often be best if learned lawmakers adopted the doctors' oath: *primum non nocere*—first, do no harm. Our first Congress (1789-91) was perhaps the most productive and significant. It concluded the American Revolution and stabilized the new government. The first Congress passed the first 10 amendments, the Judiciary Act of 1789 and acts establishing the first three executive departments, the creation of a revenue system, the admission of two new states, the approval of the Secretary of the Treasury's plan for funding the foreign, domestic and state Revolutionary War debts, established the national bank, and decided on the location of the U.S. capital city. For a great history, read Robert Remini's *The House—The History of the House of Representatives*.

**Habeas Shmabeas: Islamic Jihadists, Child Rapists and the Supreme Court.** Speaking of doing no harm and 'lawmakers,' the Supreme Court should follow *primum non nocere* and take more vacation time, perhaps adding Winter to their three-month Summer break.

I admit that the Court tried very hard not to work. During its 2007-2008 term, the Court issued only 72 opinions. This averages to eight opinions per Justice. Eight is also the number of law clerks assigned to each Justice. Given the limited work and the ample corps of clerks, the Justices filled their time by writing 150-page opinions with lots of footnotes.

Twenty-eight of the Slip Opinions (38% of the workload) came out between June 2 and June 26, 2008. I guess the Justices had non-refundable vacation tickets. During the other three months of work, the Court issued 44 opinions.

You figure with that light load, they could not screw things up. But remember the saying: "Idleness is the root of mischief." Without *Clinton v. Jones*, *Bush v. Gore* or Ken Starr, the Court decided to branch out into military matters. Why not? If they can write 72 opinions, how hard is to wage war? By a 5/4 vote the Court ruled that "alleged" terrorists captured by the U.S. military in Afghanistan or some other -istan that were transferred to Guantanamo Bay Naval Base (located on the island controlled by the Latin American Mugabe) have *habeas corpus* rights in federal courts, the same places we file and defend lawsuits. All I can say is I sure hope those federal court metal detectors work. Hmmm, 72 opinions; 72 virgins? Coincidence?

By the same 5/4 split, the Court ruled that a state's death penalty is unconstitutional as applied to a convict who raped, but did not kill, a child. At least the Europeans must love us, after we show them that terrorists and child rapists are humans, too!

Four of the five Justices — who ruled in favor of those seeking spiritual "enlightenment" in Tora Bora terror camps (not Bora Bora resorts) and child rapists — would imprison Americans in the Nation's capitol for owning a handgun or keeping an unloaded shotgun in their own homes! Guns don't kill people; terrorists do. *Primum non nocere*.

— John G. Adam

# GOVERNMENT EMPLOYEES RUNNING FOR PUBLIC OFFICE: LOOK BEFORE YOU LEAP OR FACE TROUBLE UNDER THE HATCH ACT

Jason C. Miller

It happens every two years. An employee of a local or state government agency decides to run for political office on his or her own time only to find out that he will lose his job if he actually files to run for office. What could have been an election fight turns into an employment dispute. Unless the employee properly plans ahead of time, in this dispute a federal agency is, in effect, vested with the authority to order the employee discharged by the local agency.

The Office of Special Counsel (OSC) in Washington, D.C. is charged with enforcing the Hatch Act. The Hatch Act, as amended, substantially limits political activities of federal employees and prohibits state and local government employees who are principally employed in a position that receives federal funding from running for partisan political office. 5 U.S.C. § 7323(a)(3) (federal); 5 U.S.C. § 1502(a)(3) (state and local). Certain private nonprofits, specifically the Community Action Agencies that run Headstart programs, are also brought under the Hatch Act as a condition of their federal grants. 42 U.S.C. § 9918(b)(1); 42 U.S.C. § 9851(a).

The Act also contains more generalized anti-corruption provisions that prevent the abuse or misuse of official power. 5 U.S.C. § 7323(1)-(2)(federal); 5 U.S.C. § 1502(a)(1)-(2) (state and local). Criminal violations are possible for the most egregious political abuses. *See, e.g.*, 18 U.S.C. § 594. However, a covered employee who runs for office will either be forced to withdraw from the race or, depending on the circumstances, be terminated from his job. 5 U.S.C. § 7326.

In Michigan state and county government positions are partisan, though most city governments and school board positions are nonpartisan. The result being that, based on fears of corruption, a covered employee cannot run for Putnam Township Trustee, a partisan office, but can run for Mayor of Detroit, a nonpartisan office. 5 U.S.C. § 1503 (nonpartisan candidacies permitted).

There are notable distinctions between federal, state and local, and education and research employees. The ban on federal employees running for partisan office is effectively absolute. State and local government employees only face Hatch Act restrictions if their position receives federal funding and they exercise functions related to that federally funded activity. 5 U.S.C. § 1504(4)(A). Likewise, employees of state and private education and research institutions, like teachers and professors, are not covered by the Hatch Act. 5 U.S.C. § 1501(4)(B).

There are over 20 million civilian government employees at all levels.<sup>1</sup> Many of them have an interest in running for office and some of them are arguably especially qualified to hold public office by virtue of their government experience. The Constitution does protect these employees against coercion based on politics. *Rutan v. Republican Party*, 497 U.S. 62 (U.S. 1990) (low-level government employees may not be discharged based on political affiliation). However, the Supreme Court has upheld the constitutionality of the Hatch Act as a legitimate restriction on employee speech. *U.S. Civil Service Commission v. National Association of Letter Carriers*, 413 U.S. 548 (1973); *see also Carver v. Dennis*, 104 F.3d 847, 851 (6th Cir. 1997) (candidacy not a fundamental right).

The Hatch Act often comes as a surprise to state and local government employees because it is a federal regulation. Federal employees are more likely to have heard of the Act. Many local government employees do not realize that their positions are associated with federal funding. Even a small federal grant, comingled with office administration and salaries, brings them within the Act's coverage.

The employee need not be principally funded by the federal government, only principally employed in a position that federal dollars touch. With so many federal programs involving grants or aid to state and local agencies, few local government employees can be certain they are not covered by the Act. A sheriff's deputy and a city police officer are both under investigation in Lenawee County for running for an open county sheriff position.<sup>2</sup>

The one set of government employees who are almost always safe are elected incumbents. When an individual's only contact with the federal dollars comes by virtue of holding an elected position, he or she is not prohibited from running for partisan office. 5 U.S.C. § 1502(c). Ironically, an incumbent prosecutor can run for re-election, but may use the Hatch Act to fire her subordinate assistant prosecutor for running against her, as happened this year in Mason County, Michigan.<sup>3</sup> Courts have considered and rejected a rational-basis challenge to the distinction between incumbents and non-incumbents.<sup>4</sup>

Some candidates will be terminated, some will voluntarily resign their job, and many will withdraw their candidacy. The OSC notes that Hatch Act prosecutions and investigations have been increasing in recent years. However, most matters will never make the news or even be investigated – the covered employee will find out about the threat to his or her employment and quietly bow out of the race. Government employees have to live within the confines of the Hatch Act and work around it if they hope to win public office.

An attorney who is approached by a concerned state or local government employee, or perhaps is one herself, considering running for public must first discern whether the employment involves any degree of federal funding. Some positions are clearly federally-funded, but complicated government funding may be less obvious in other positions. Employees may not even be aware of small federal grants, like those frequently received by local law enforcement agencies for specific projects. The employee likely thinks of himself as a county or township, not a federal, employee.

The OSC staff will answer informal questions and is authorized by statute to issue advisory opinions. 5 U.S.C. § 1212(f). The employee should request documents and budget details to enable the OSC to determine whether he or she is covered under the Act. The OSC answers frequently asked questions and posts past advisory opinions on their website, which may be helpful because the same issues frequently arise.<sup>5</sup>

It is important for a potentially-covered employee to think about these issues before running for office. By examining all sources of funding for the position and activities carried out, and whether the office she hopes to seek is partisan or nonpartisan, an employee can identify her status under the Act ahead of time, allowing the employee to potentially change positions or departments within a state or local agency to avoid coverage under the Act. Or the employee may decide not to run at all. Either way, by discovering these issues ahead of time an employee can avoid the public embarrassment of being forced to lose a valued job or abandon a political campaign.

— END NOTES —

<sup>1</sup>Compendium of Public Employment: 2002 (Issued September 2004), United States Census Bureau, available online: <http://www.census.gov/prod/2004pubs/gc023x2.pdf>.

<sup>2</sup>"Two sheriff candidates under Hatch Act Review" Dennis Pelham, (Adrian, MI) *Daily Telegram*, May 28, 2008, available online at: <http://www.lenconnect.com/news/x784973509/Two-sheriff-candidates-under-Hatch-Act-review>

<sup>3</sup>"Candidacy costs chief asst. prosecutor his job" Steve Bednoche, *Ludington Daily News*, May 20, 2008, available online at: [http://www.ludingtondailynews.com/news.php?story\\_id=40162](http://www.ludingtondailynews.com/news.php?story_id=40162)

<sup>4</sup>*Crespo v. U.S. Merit Systems Protection Board*, 486 F.Supp.2d 680, 693-694 (N.D. Ohio 2007). The court only considered whether an incumbent would have to resign to run for re-election to the post he was currently holding. *Id.* They did not consider the irrationality of an elected prosecutor and an assistant prosecutor being treated differently if both were running for Congress.

<sup>5</sup>*See* <http://www.osc.gov> or call (800)85-HATCH. ■



## INSIDE LAWNOTES

- Sue Ellen Eisenberg explains the impact of Internal Revenue Code Section 409A on severance agreements.
- KOHP lawyers Margaret Alli, Tom Kienbaum, and Sonja Lengnick write on FLSA, retiree health care litigation, and NLRA governance of non-union employees.
- Stuart Israel reviews *Lawnotes* columnist Barry Goldman's new book, *The Science of Settlement — Ideas for Negotiators* and Doug Bonney addresses opening statements.
- Joe Marutiak meditates on the relationship between the NLRB and Tibetan sand mandalas and Bill Saxton reviews the practical implications of the Supreme Court's *CBOCS* decision.
- Stacy Hickox reviews the manager and supervisor FLSA exemptions and John Holmquist assesses the Supreme Court's *Mendelsohn* decision.
- Star Swift and Kathy VanDagens detail web resources for labor and employment lawyers.
- Labor and employment decisions from the U.S. Supreme Court, the Sixth Circuit, the Eastern and Western Districts, the Michigan Supreme Court and Court of Appeals, the NLRB and MERC, MIOSHA, MDCR and EEOC news, websites to visit, a cartoon by Maurice Kelman, and more.
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