806:Employment Law Year in Review

Michael J. Lotito
Partner
Jackson Lewis LLP

Dana M. Muir
Associate Professor of Business Law
University of Michigan Business School

Patti E. Russell
Associate General Counsel and Senior Employment Counsel
Becton, Dickinson and Company

Faculty Biographies

Michael J. Lotito

Michael J. Lotito is a partner at Jackson Lewis, a law firm that specializes in preventive labor, employment, immigration, and benefits law, representing management since its founding. Mr. Lotito has devoted his entire professional career to representing management interests in employment law. He has worked tirelessly to counsel management on understanding and adhering to the law and in resolving employment issues quickly and fairly.

A top-rated speaker and presenter, Mr. Lotito has keynoted many conferences throughout the world. Most recently he was honored as a member of TEC 200, a designation that places him among the top 1% of all TEC presenters. Mr. Lotito has coauthored several books on the ADA including *The Americans with Disabilities Act: A Comprehensive Guide to Title I.* Additionally, he sits on the board for Sterling Testing Systems, a nationwide pre-employment screening company based in New York.

He is a past chair of the Society of Human Resource Management and was chairman of SHRM's national legislative affairs committee. He has testified before the U.S. Senate and House of Representatives. He has been elected as a Fellow to the ABA.

Mr. Lotito graduated from Villanova University and then Villanova Law School.

Dana M. Muir

Dana M. Muir is an associate professor of business law at the University of Michigan Business School. She teaches a variety of MBA and executive education courses, including courses in employment law. She also periodically teaches employee benefits law at the University of Michigan Law School. Professor Muir has published numerous articles in law reviews, legal journals, and conference proceedings. In 2002 the United States Supreme Court cited her research in a decision on ERISA remedies.

Prior to joining UMBS, she practiced law at Winston & Strawn and at Dykema Gossett. In addition, she has held numerous positions in human resources at the Chrysler Corporation, including in corporate compensation, benefits, and staff personnel.

Professor Muir currently serves on the Department of Labor's ERISA Advisory Council and is active in the ABA's employee benefits programs. In fall 2000, Professor Muir worked as a Congressional Fellow.

Professor Muir received her law degree from The University of Michigan Law School where she was on the editorial board of the *Michigan Law Review,* and she also holds an MBA.

Patti E. Russell

Patti E. Russell is associate general counsel for Becton, Dickinson and Company (BD) in Franklin Lakes, New Jersey. As chief employment counsel, she advises senior management on all

workplace/human resources issues, manages civil litigation, and ensures EEO compliance. Ms. Russell also is a member of BD's diversity task force, and leads two of its subcommittees. At BD, Ms. Russell is responsible for all employment and labor matters, including employee relations matters, employment, separation and related agreements, policy issues, employee misconduct and investigations, reorganizations and reductions in force, compensation and benefits, and employment issues relating to mergers and acquisitions. She also represents the company in employment and general litigation. Ms. Russell also counsels senior management and the company's ethics officer and director of security on a variety of general legal issues and negotiates commercial agreements.

Prior to joining BD, Ms. Russell was a litigation associate with McCarter & English in Newark, New Jersey, representing corporate and nonprofit clients in a variety of areas, including commercial law, employment and labor matters, education law, and product liability.

Ms. Russell currently serves as a member of the legal affairs committee of the New Jersey Business and Industry Association. As a volunteer attorney, she provides counsel to nonprofit organizations through the Pro Bono Partnership. She also lectures both internally as a member of BD University's faculty and externally at seminars on various topics.

Ms. Russell received a BS from Cornell University and is a graduate of New York University School of Law.

ACCA 2003 Annual Meeting
Charting a New Course

Employment Law Year in Review:

Finding Fair Winds in a Sea of New Workplace Laws and Regulations

Michael J. Lotito, Esq.
Jackson Lewis LLP

Legislative and Regulatory Update 2002 -- 2003

- Department of Labor's proposed Fair Labor Standards Act regulations for "white collar" exemptions
- Occupational Safety and Health Administration's enhanced enforcement initiatives
- Federal Family and Medical Leave Act proposed modifications and California paid leave
- National Labor Relations Act preemption of state "neutrality" laws
- Health Insurance Portability and Accountability Act "Privacy Rule"

Labor Department Proposes Changes to 50-year Old Wage and Hour Rules on Exempt Employee Status

(http://www.jacksonlewis.com/publications/articles/20030401/default.cfm)

On March 31, 2003, the U.S. Department of Labor, Wage and Hour Division issued Proposed Rules and Request for Comments regarding modifications to the definitions of exempt employees under the Fair Labor Standards Act (29 C.F.R. § 541). The proposed regulations will be used to determine the exemptions for executive, administrative, professional, outside sales and computer employees, often referred to as the "white collar" exemptions. "Updating these regulations is long overdue-the types of jobs people do and the skills they need have changed, but the regulations have not," said Wage and Hour Administrator Tammy D. McCutchen when announcing the proposals. "The exemptions have engendered considerable confusion over the years regarding who is, and who is not, exempt," McCutchen wrote in issuing the proposed regulations.

Why the Rules Needed Changing

It should be noted that the proposed regulations do not change the basic requirements for determining the exempt or non-exempt status of employees. Rather, the changes are designed to respond to the current workplace reality in which the basic requirements must be applied.

Under the current rules, to be exempt from the FLSA's overtime requirements, an employee: 1) must be paid a guaranteed salary which is not subject to reductions because of variations in the quality or quantity of work performed (known as the "salary basis test"); 2) must receive at least the minimum guaranteed salary set forth in the regulations (the "salary level test"); and, 3) must perform primarily "managerial, administrative or professional duties as outlined in the regulations" (known as the "duties test").

Originally established in 1938, the duties tests for the executive, administrative, and professional white collar employees were last modified in 1949. Similarly, the salary basis test has been unchanged since 1954, and salary levels were last updated in 1975.

The regulations were in need of updating not only because more than 50 years have elapsed since parts of the current regulations were last modified, but even more importantly because they are functionally outdated. The salary level tests are particularly problematic since they were intended to be the best indicators of exempt status. At current levels, they no longer assist employers in distinguishing between *bona fide* exempt employees and those who should be considered non-exempt.

As currently written and applied, the complex "duties" tests often result in error and subsequent misclassification of employees, and the subjective nature of the "duties" tests has resulted in inconsistent application of the exemptions by investigators and

by the courts. Additionally, the complex "salary basis" tests and the so-called "no docking" rule have been the subject of numerous collective court actions brought against employers by highly compensated managerial and professional employees.

Summary of Significant Proposed Changes

As proposed, the new rules would affect nearly every major aspect of the exempt status criteria. A useful side-by-side comparison of the existing rule and proposed changes appears at http://www.dol.gov/_sec/media/speeches/541_Side_By_Side.htm on the Department of Labor website.

If the proposed changes are accepted, the final rule would have the following impact:

Increase the salary levels tests.

Under the proposed regulations, the minimum salary level for an executive, administrative or professional employee to qualify for exempt status would be increased from $155.00 to $425.00 per week (see discussion below).

Eliminate separate "long" and "short" salary level and duties tests.

The proposal eliminates the current percent limitation on non-exempt work and the requirement that employees must exercise independent judgment or discretion, and substitutes one standard test.

For Executive Employees, Subpart B, §§ 541.100 - 107

To qualify as exempt under the duties test, an executive employee must:

1. as a primary duty, manage the enterprise in which the employee is employed or a customarily recognized department or subdivision;
2. customarily and regularly direct the work of two or more other employees; and
3. have the authority to hire or fire other employees or have particular weight given to suggestions and recommendations as to hiring, firing, advancement, promotion or any other change of status of other employees.

Any employee who owns at least a 20% equity interest in the enterprise would be recognized as exempt.

For Administrative Employees, Subpart C, §§ 541.200 - 207

To qualify as exempt under the duties test, an administrative employee must:

- as a primary duty, perform office or non-manual work related to management or general business operations of the employer or the employer's customers;

- hold a position of responsibility with the employer. To meet this requirement the employee must customarily and regularly (1) perform work of substantial importance; or (2) perform work requiring a high level of skill or training.

The proposed rules clarify the type of work performed that will be considered to be "office or non-manual work." Illustrative examples included in the proposed regulations are:

a. Tax

b. Finance

c. Accounting

d. Auditing

e. Quality control

f. Purchasing

g. Procurement

h. Advertising

i. Marketing

j. Research

k. Safety and Health

l. Personnel Management

m. Human Resources

n. Employee Benefits

o. Labor Relations

p. Public Relations

q. Government Relations

The proposed rules define the "position of responsibility" requirement. The DOL intends to reduce the emphasis that has been placed upon the "production versus staff" dichotomy when differentiating between exempt and non-exempt workers. To

meet this requirement, the employee must customarily perform work (1) of substantial importance or (2) requiring a high-level of skill.

The requirement that an employee perform work of "substantial importance" has been a part of the interpretive guidelines for the administrative exemption since 1950. Work of substantial importance is defined to mean "work that, by its nature or consequence, affects the employer's general business operations or finances to a significant degree." The proposed regulations include the following examples of this type of activity:

- formulating, interpreting or implementing management policies
- providing consultant or expert advice to management
- making or recommending decisions that have a substantial impact on general business operations or finances
- analyzing and recommending changes to operating practices
- planning long and short tem business objectives
- analyzing data, drawing conclusions and recommending changes
- handling complaints, arbitrating disputes or resolving grievances
- representing the employer during important contract negotiations

Addressing the other prong of the "position of responsibility" requirement, the proposed rules define "work requiring a high level of skill or training" as work requiring specialized knowledge or abilities or advanced training. The requisite knowledge or abilities can be acquired through academic instruction or advanced on-the-job training. The proposed regulations reverse the DOL's previous view that use of a reference manual was indicative of non-exempt duties. Under the proposed regulations, use of a manual which contains highly technical, scientific, legal, financial or similarly complex information that *can be interpreted only by those with advanced training or specialized knowledge or skills* will be regarded as exempt work.

For Professional Employees, Subpart D, §§ 541.300 - 304

To qualify as exempt under the duties test, a learned professional employee must as a primary duty, perform office or non-manual work requiring advanced knowledge in a field of science or learning, which is:

- customarily acquired by a prolonged course of specialized intellectual instruction; or
- acquired through equivalent combinations of intellectual instruction and work experience.

The proposed rules clarify the professional exemption by recognizing that, in the "modern workplace," employees can acquire advanced knowledge through a combination of formal college-level education, training *and* work experience. Under the current regulations, the advanced knowledge requirement was most typically satisfied through academic instruction *rather than* knowledge gained through work experience.

The proposed regulation also recognizes that the areas covered by the professional exemptions "are expanding." Subpart § 541.301(g) provides that whenever a specialized degree becomes a standard requirement for a particular occupation, that occupation could be considered a "learned profession" and could qualify for the professional exemption.

To qualify for the exemption for creative professional employee, an individual must, (1) as a primary duty, perform office or non-manual work requiring invention, imagination, originality or talent; and, (2) do so in a recognized field of artistic or creative endeavor such as music, writing, acting or the graphic arts.

Uncertainty in the existing rules for creative professional employees has spawned litigation over a number of occupations, including newspaper journalists and radio or television commentators. The proposed rules recognize that writers for newspapers, magazine, television, the internet, and other media generally perform work requiring originality and talent. In these occupations, exempt work includes conducting interviews, reporting or analyzing public events and acting as a narrator, announcer or commentator.

For Computer Employees, Subpart E

The proposed regulations relocate the computer related exemption from within the professional exemption to a separate exemption. The new section consolidates all the provisions from the current regulations, interpretive guidance and the legislative enactments. The proposal increases the minimum salary requirement to $425.00 per week or, on an hourly basis, requires payment at a rate of not less than $27.63 an hour.

For Outside Sales, Subpart F, §§ 541.500 - 504

The proposed regulations eliminate the current 20% restriction on non-exempt work. Under the proposed rules, the exemption would apply when the employee's primary duty is making sales, or obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer. The employee also must be customarily and regularly engaged away from the employer's place or places of business.

Compensation Requirements, Subpart G, §§ 541.600 - 606

The proposed regulations increase the minimum salary requirement to $425.00 weekly for the new "standard" test for the executive, administrative and professional exemption. The DOL established the minimum salary by looking at the Bureau of Labor Standards year 2000 Current Population Survey Outgoing Rotations Data Set. Based upon its review, the DOL has suggested setting the minimums at the lowest 20% of the current range of salaries. As a result, the bottom 20% of salaried employees would fall below the minimum salary and would be entitled to overtime.

Subpart § 541.601 of the proposed rules introduces a special test for highly compensated employees. Under this "super salary" test, employees would qualify for the executive, administrative or professional exemptions if they:

1. perform office or non-manual work;
2. are guaranteed total annual compensation of at least $65,000; and,
3. perform one or more of the exempt duties of an executive, administrative and professional employee as set forth in the proposed regulations.

When determining whether an employee is highly compensated, the employer may consider base salary, commissions and *non-discretionary* compensation (including bonuses).

For employees who have not worked a full year, the proposed rules allow an employer to pro rate earnings and attribute a *pro rata* portion of the minimum earnings required. Based upon the number of weeks he or she has been employed, the employee may qualify for the "super salary" exemption.

Salary Basis, Subpart G

One of the most contentious areas of exempt status in recent years has involved the loss of exemptions as a result of improper salary deductions. The proposed rules add a provision allowing employers to take deductions for full-day disciplinary suspension for infractions of workplace conduct rules, such as sexual harassment policies.

Additionally, the proposed rules significantly alter the "window of correction" which provides an employer the opportunity to fix a mistake in salary deductions from exempt employees. Under the proposed rules, an employer will lose an otherwise valid exemption if there is a *pattern and practice* of making improper deductions and, as a result, not paying employees on a "salary basis." In contrast, if the deductions are isolated or inadvertent, an otherwise valid exemption will not be lost. Factors to consider include:

- the number of improper deductions;
- the time period during which deductions were made;
- the number and geographic location of employees whose salary was improperly reduced;
- the size of the employer;
- whether the employer has a written policy prohibiting improper deductions; and,
- whether the employer corrected the improper deductions.

Significantly, if the facts show the employer has a policy of not paying on a salary basis, the exemption is lost only during the time period in which improper deductions were made for employees *in the same job classifications working for the same managers responsible for the improper deduction*.

The proposed rules also provide "a safe harbor" that the exemption will not be lost if the employer (1) has a written policy prohibiting improper pay deductions; (2) notifies employees of its policies; and, (3) reimburses employees for any improper deductions. However, if the employer repeatedly and willfully violates its own policy or continues to make deductions after receiving employee complaints, the exemption will be lost.

Definitions, Subpart H

Definitions for the terms used in the proposed regulations are consolidated into one section. The proposed rules define "primary duty" as the major or most important duty the employee performs. The regulations provide some guidance on the determination of an employer's primary duty. Some of the factors to be considered:

1. the relative importance of the exempt duties as compared with other duties;
2. the amount of time spent performing exempt work;
3. the employee's relative freedom from direct supervision; or
4. the relationship between the salary the employee receives and wages paid to other employees for the same kind of non-exempt work.

Importantly, this definition also provides that an employee is not required to spend more than 50% of his or her time performing exempt work to sustain the primary duty test.

Tasks that are "directly and closely related" to exempt duties also may be considered exempt work. This includes physical or menial tasks that arise out of exempt duties, and routine work without which the employee's exempt duties cannot be performed. Examples include keeping time; preparing production or sales records for subordinates; spot checking the work of subordinates; recordkeeping; monitoring and adjusting machinery; taking notes; using a computer to create documents or presentations; opening mail for the purpose of reading it and making decisions.

Emergencies, § 541.705

This portion of the regulations recognizes that emergencies may arise that require an exempt employee to perform work of a non-exempt nature. If such emergencies (1) threaten the safety of employees; (2) could cause cessation of operations; or (3) present the risk of serious damage to the employer's property, the work performed to prevent such results will be considered exempt.

Comments Requested in Troublesome Areas

The DOL invited public comments on the proposed rules specifically related to occupations that have been the subject of confusion and litigation regarding their exempt status, including:

- pilots
- athletic trainers
- funeral directors
- insurance salespersons
- loan officers
- stock brokers
- hotel sales and catering managers
- dietary managers in nursing homes

Other specified areas of inquiry included:

1. Whether the salary level and/or salary basis requirements should be eliminated as unnecessary for *sole charge* executives and business owners.
2. The list of type of work that constitutes office or non-manual work related to the management or general business operations.
3. The list of activities in § 541.204 that are considered to be of "substantial importance" in terms of additions or deletions to the list.
4. Whether the "discretion and independent judgment" requirement should be deleted entirely, retained as a third alternative for meeting the "position of responsibility" requirement, or retained *but modified* to provide better guidance.
5. Whether the requirements for professional exemption should include a specific formula for determining the equivalent of intellectual instruction and work experience.
6. Whether the special salary levels should be maintained for American Samoa.
7. The proposed salary levels and any alternative salary level amounts or methodologies for determining appropriate salary levels.
8. Whether the regulations should include a "salary only" test for highly compensated employers, where employees performing non-manual or office work and earning a specific amount automatically would be exempt without regard to the employee's duties.
9. Alternative strategies for removing the "salary tests" from the regulations and replacing them with tests that rely solely on employees' duties.

Raising the salary level test to $425.00 per week is just one of the changes that will impact employers in the classification of employees as exempt or non-exempt under the FLSA. Another is the establishment of the so-called super salary level test automatically to classify an employee as exempt. Perhaps the more far reaching changes involve modifications to the "duties tests." Indeed, the DOL estimates that 640,000 employees would be affected by these proposed modifications, which include eliminating the percentage test for duties performed of a non-exempt nature.

While the response to the proposed regulations thus far has been mixed and the outcome is uncertain -- prior attempts to revise the "white collar" regulations have failed -- McCutchen has stated that if she "gets a little bit of screaming" from both labor and business groups, "then I'll think I probably found the right solution."

U.S. Department of Labor
(http://www.dol.gov/_sec/media/speeches/541_Side_By_Side.htm)

U.S. Department of Labor Proposal to Strengthen Overtime Protection

Side-By-Side Comparison

The following charts compare the current requirements for exemption from the Fair Labor Standards Act as an executive, administrative, professional, computer or outside sales employee with the regulations proposed by the Department of Labor.

Executive Employees

	Current Long Test	Current Short Test	Proposed Standard Test
Salary	$155 per week	$250 per week	$425 per week
Duties	Primary duty of the management of the enterprise or a recognized department or subdivision. Customarily and regularly directs the work of two or more other employees. Has authority to hire or fire other employees (or recommendations as to hiring, firing, promotion or other change of status of other employees are given particular weight). Customarily and regularly exercises discretionary powers. Does not devote more than 20 percent (40 percent in retail or service establishments) of time to activities that are not directly and closely related to exempt work.	Primary duty of the management of the enterprise or a recognized department or subdivision. Customarily and regularly directs the work of two or more other employees.	Primary duty of the management of the enterprise or a recognized department or subdivision. Customarily and regularly directs the work of two or more other employees. Has authority to hire or fire other employees (or recommendations as to hiring, firing, promotion or other change of status of other employees are given particular weight).

Administrative Employees

	Current Long Test	Current Short Test	Proposed Standard Test
Salary	$155 per week	$250 per week	$425 per week
Duties	Primary duty of performing office or non-manual work directly related to management policies or general business operations of the employer or the employer's customers. Customarily and regularly exercises discretion and independent judgment. Regularly and directly assists a proprietor, or exempt executive or administrative employee; o*r* performs specialized or technical work requiring special knowledge under only general supervision; *or* executes special assignments under only general supervision. Does not devote more than 20 percent (40 percent in retail or service establishments) of time to activities that are not directly and closely related to exempt work.	Primary duty of performing office or non-manual work directly related to management policies or general business operations of the employer or the employer's customers. Customarily and regularly exercises discretion and independent judgment.	Primary duty of performing office or non-manual work directly related to the management or general business operations of the employer or the employer's customers. Holds a "position of responsibility" with the employer, defined as either (1) performing work of substantial importance or (2)performing work requiring a high level of skill or training.

Learned Professional Employees

	Current Long Test	Current Short Test	Proposed Standard Test
Salary	$170 per week	$250 per week	$425 per week
Duties	Primary duty of performing work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study. Consistently exercises discretion and judgment. Performs work that is predominantly intellectual and varied in character and is of such character that the output produced or result accomplished cannot be standardized in relation to a given period of time. Does not devote more than 20 percent of time to activities that are not an essential part of and necessarily incident to exempt work.	Primary duty of performing work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction and study. Consistently exercises discretion and judgment.	Primary duty of performing office or non-manual work requiring knowledge of an advanced type in a field of science or learning customarily acquired by a prolonged course of specialized intellectual instruction, but which also may be acquired by alternative means such as an equivalent combination of intellectual instruction and work experience.

Creative Professional Employees

	Current Long Test	Current Short Test	Proposed Standard Test
Salary	$170 per week	$250 per week	$425 per week
Duties	Primary duty of performing work that is original and creative in character in a recognized field of artistic endeavor, and the result of which depends primarily on the invention, imagination, or talent of the employee. Consistently exercises discretion and judgment. Performs work that is predominantly intellectual and varied in character and is of such character that the output produced or result accomplished cannot be standardized in relation to a given period of time. Does not devote more than 20 percent of time to activities that are not directly and closely related to exempt work.	Performs work requiring invention, imagination, or talent in a recognized field of artistic endeavor.	Primary duty of performing work requiring invention, imagination, originality or talent in a recognized field of artistic or creative endeavor.

Computer Employees

	Current Long Test	Current Short Test	Section 13(a)(17) Test	Proposed Standard Test
Salary	$170 per week	$250 per week	$27.63 an hour	$425 per week *or* $27.63 an hour
Duties	Primary duty of performing work requiring theoretical and practical application of highly-specialized knowledge in computer systems analysis, programming, and software engineering. Employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer software field. Consistently exercises discretion and judgment. Performs work that is predominantly intellectual and varied in character and is of such character that	Primary duty of performing work requiring theoretical and practical application of highly-specialized knowledge in computer systems analysis, programming, and software engineering. Employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer software field. Consistently exercises discretion and judgment.	Primary duty of (A) application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional applications; *or* (B) design, development, documentation, analysis, creation, testing, or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications; *or* (C) design, documentation, testing, creation or modification of computer programs	Primary duty of (A) application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software or system functional applications; *or* (B) design, development, documentation, analysis, creation, testing, or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications; *or* (C) design, documentation, testing, creation or modification of computer programs

	character that the output produced or result accomplished cannot be standardized in relation to a given period of time. Does not devote more than 20 percent of time to activities that are not directly and closely related to exempt work.		related to machine operating systems; *or* (D) a combination of duties described in (A), (B) and (C), the performance of which requires the same level of skills. Employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer field.	related to machine operating systems; *or* (D) a combination of duties described in (A), (B) and (C), the performance of which requires the same level of skills. Employed as a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker in the computer field.

Outside Sales Employees

	Current Long Test	Current Short Test	Proposed Standard Test
Salary	None required.	None required.	None required.
Duties	Employed for the purpose of and customarily and regularly engaged away from the employer's place of business in making sales; *or* in obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer. Does not devote more than 20 percent of the hours worked by nonexempt employees of the employer to activities that are not incidental to and in conjunction with the employee's own outside sales or solicitations.	No separate "short" test.	Primary duty of making sales; *or* of obtaining orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer. Customarily and regularly engaged away from the employer's place or places of business.

Jackson Lewis Assists ACCA in Preparing Comments to the DOL Proposed FLSA Rule Changes

ACCA's Labor & Employment Law Committee Comments on Proposed Revisions to FLSA Rules

While media coverage predictably has written a management versus worker story, ACCA's Labor and Employment Law Committee's comments, in response to the Department of Labor's proposed revisions of the FLSA overtime rule, find a middle ground that praises that which is good in the proposed rule, urges the Department to do better in other areas and submits serious proposals for consideration and/or inclusion in the final regulation.

The complete Comment includes two exhibits. Exhibit A is a draft definition of the administrative exemption incorporating ACCA's proposed revisions while Exhibit B lists descriptions of job positions proposed for inclusion in the final rule.

Click here for the Comments and Exhibit A (http://www.acca.com/networks/lelaw/exhibit_a.pdf). Click here for Exhibit B (http://www.acca.com/networks/lelaw/exhibit_b.pdf).

These comments were prepared with the assistance of Jackson Lewis, LLP, the 2003 sponsor of ACCA's Labor & Employment Law Committee, and David Fortney, Esq. Of Fortney & Scott.

(reproduced from ACCA Labor & Employment Law Committee website at www.acca.com/networks/lelaw.php)

OSHA Issues Alerts to Over 14,000 Employers With Elevated Injury and Illness Rates

(http://www.jacksonlewis.com/publications/articles/20030304/default.cfm)

On February 24, 2003, OSHA announced it would be contacting over 14,000 employers to alert them that their recent injury and illness rates are above the national average and suggesting they act to decrease the hazards faced by their employees. Although this is not the first time OSHA has issued such "alerts," it is the first time the Agency has included construction industry employers in the notifications.

The list of employers chosen to receive this letter was drawn from the results of OSHA's illness and injury survey for 2001. The survey covered 93,000 employers, including, for the first time, 13,000 construction companies. Notices were sent to all employers reporting six or more lost workday injuries or illnesses per 100 employees in 2001. The national average for the year was just under three lost workdays. The alert to each company, which is signed by OSHA Administrator John Henshaw, includes the company's actual injury and illness statistics and explains:

"This means employees in your business are being injured at a higher rate than in most other businesses in the country. I am writing you to indicate my concern about the high LWDII [lost work day illness and injury] rate at your establishment and to identify ways that you can obtain assistance in addressing hazards in your workplace.

The Administrator offers suggestions for improving the company's rates and includes a list of standards most frequently violated by the relevant industry. OSHA's official press release regarding this development includes the following quote from Administrator Henshaw:

Armed with this information, we'll not only be able *to place our inspection resources where they're most needed*, but we can also use the information to plan outreach and compliance assistance programs where they will benefit the most.

The italicized part of this comment refers to OSHA's practice of conducting what it terms "programmed inspections." This means the Agency will select an undisclosed number of employers from the 14,000 who will be given a high priority for inspection in the upcoming year.

The complete list can be viewed at OSHA's website, http://www.osha.gov/as/opa/foia/hot_9.html. The establishments are grouped by state and listed alphabetically. Because the survey was a federal OSHA project, establishments in states that have opted to implement state enforcement programs, commonly called "state-plan states," were not included in the survey and do not

appear on the list. The SIC (Standard Industrial Classification) codes for the establishments included in the survey are set out in the table below:

15 - 17 Construction

20 - 39 Manufacturing

018 Horticultural Specialties

021 Livestock (except Dairy and Poultry)

024 Dairy Farms

025 Poultry and Eggs

027 Animal Specialties

0291 General Farms, primarily animal

0783 Ornamental Shrub and Tree Services

421 Trucking and Courier Services (except Air)

422 Public Warehousing and Storage

423 Trucking Terminal Facilities

4311 U.S. Postal Service

449 Water Transportation Services

451 Air Transportation, Scheduled

458 Airports, Flying Fields, and Services

4783 Packing and Crating

4953 Refuse Systems

501 Motor Vehicles and Motor Vehicle Parts and Supplies

503 Lumber and Other Construction Materials

505 Metals and Minerals (except Petroleum)

5093 Scrap and Waste Materials

514 Groceries and Related Products

518 Beer, Wine, and Distilled Beverages

5211 Lumber and Other Building Materials

5311 Department Stores

805 Nursing and Personal Care Facilities

806 Hospitals

OSHA Combines Employer List with Site Specific Targeting in New Enforcement Initiative

(http://www.jacksonlewis.com/publications/articles/20030317/default.cfm)

The Occupational Safety and Health Administration has announced an important new enforcement policy targeting 10,000 specific employers for more robust workplace inspections that may result in heavy citations, expanded penalties, and continuing governmental scrutiny. OSHA's new strategy announced on March 11 is part of the agency's reinvigorated efforts to force employers to improve their safety records. To be prepared for this new enforcement scheme, employers with targeted facilities should analyze their vulnerability to an OSHA inspection and develop a response strategy that includes compliance with existing OSHA standards and addresses agency guidance on previously identified hazards.

The 10,000 employers are listed by means of over 14,200 individual "establishments" (i.e., individual plants, facilities, locations, etc.) having what OSHA has recently identified as excessive injury and illness rates (see discussion above). Identifying employers on the basis of an individual establishment's safety record, as opposed to an overall company record, exposes many companies with exceptional overall safety records to the enhanced enforcement and remedial measures reserved for the "targeted employer" list.

In addition to enhanced inspections, new punitive measures under the enforcement initiative are triggered by an OSHA finding that an identified establishment has a "high gravity" violation. For example, a finding of a "high gravity" violation could be expected in the event of a fatality at a facility.

Under the OSHA Site Specific Targeting (SST) Program, the identified establishments will be assigned a high priority for inspection in 2003 and early 2004. **If a "high gravity" violation is identified in the course of an SST inspection of one identified establishment, under OSHA's new enforcement strategy *all other establishments under the same corporate identity* will be placed on the *primary* SST inspection list for this same year.** This means companies with

overall exemplary safety records or programs are at risk of being pushed to the top of the priority inspection list for all other establishments.

In addition to corporate-wide inspections, multiple penalties and interruptions to production, there are other substantial punitive consequences connected with the new enforcement initiative. OSHA Administrator John Henshaw has stated these measures are designed to "put more tenacity and teeth in our enforcement practices."

Tougher Settlement Provisions. OSHA will be more adamant in requiring employers to agree to tougher conditions for settling citations, including: (1) advance consent to submit to summary enforcement by order of the federal courts with the power to issue findings of contempt; (2) use of safety consultants with the aim of changing the establishment's "safety and health culture"; (3) corporate-wide application of the settlement's terms; (4) affirmative reporting to OSHA any future serious injury or illness that requires "outside medical treatment;" and (5) advance consent to inspections triggered in response to such reports.

Automatic Follow-Up Inspections. Any establishment cited for a "high gravity" violation automatically will be scheduled for a follow-up inspection. According to Administrator Henshaw, the agency intends to take the "discretion out of the hands of the area directors" for follow-up inspections. Targeted employers will face a cycle of multiple investigations, citations and increasing penalties.

Adverse Publicity For Employers. OSHA will issue regional and national press releases regarding enforcement actions. The agency recognizes that the media, especially local news organizations, often uses OSHA press releases as a resource for articles about local employers and believes significant pressure can be brought to bear on companies through media exposure.

In addition, there may be other consequences. Unions and disgruntled employees can be expected to use the fact that an employer has an establishment targeted by OSHA to put pressure on the company, especially in situations where a company already is involved in union organizing or collective bargaining.

If OSHA finds a "high gravity" violation at a targeted establishment, companies can expect other negative consequences. Among them will be the direct costs from any additional assessed penalties, as well as the indirect costs resulting from the significant disruption caused by additional inspections.

Obviously, it is critically important that targeted employers understand their exposure to enhanced and company-wide inspections, stiffer punitive measures, and repeated inspections as a result of OSHA's new enforcement initiative.

OSHA Notifies 14,200 Employers with Highest Injury and Illness Rates

As discussed above, employer establishments with higher than average injury and illness rates were notified by the Occupational Safety and Health Administration and

encouraged to take steps to reduce the hazards and protect workers. OSHA identified establishments with the highest lost workday injury and illness rates based on data from 2001 and reported by 93,000 employers surveyed last year. Workplaces receiving the alert letters had six or more injuries or illnesses resulting in lost workdays or restricted activity for every 100 full-time workers. Nationwide, the average U.S. workplace had just under three lost-time instances for every 100 workers.

The 14,200 sites are listed alphabetically, by state, on OSHA's website. The list does not designate those earmarked for programmed inspections, however, OSHA will utilize the list to target employers for priority inspections. Those employer establishments with the highest injury and illness rates within the jurisdiction of each OSHA Area Office will be targeted for inspection first. OSHA refers to this inspection program as its Site Specific Targeting Inspection Program, or SST.

There is a new, significant risk to every employer on OSHA's targeted list, even if the employer has only *one* establishment identified. Under OSHA's new Enhanced Enforcement Initiative, if OSHA conducts a priority SST inspection and issues a citation for a "high gravity violation" (i.e., willful, multiple serious or repeat violations, failure to abate, or serious or willful violations related to a fatality), then OSHA will put all *establishments of that employer* on its primary SST inspection list, regardless of their individual safety records. The risks - financial, PR, and otherwise - associated with this new initiative are significant (see above discussion of the Enhanced Enforcement Initiative).

Also, the sites listed are those in states covered by federal OSHA; the list does not include employers in the 21 states and two territories that operate OSHA-approved state plans covering the private sector.

New California Paid Family Leave Law Is First in the Nation

(http://www.jacksonlewis.com/publications/articles/20021001/01.cfm)

In enacting Senate Bill 1661 in September of 2002, California became the first state in the nation to mandate paid family leave. The new law expands state disability insurance coverage to provide benefits to employees who take time off to care for a covered family member or bond with a new or adopted child under the California Family Rights Act.

It is important to note the new requirements do not apply to new leaves of absence until July 2004. Additionally, it should be noted that employers do not have to "pay" employees for leave. Rather, the paid benefit is through already mandated state disability insurance, and employees are taxed via payroll deduction for the new disability benefits. Also, the bill does not impact employees who are absent from work due to their own serious health condition. They are already entitled to state disability insurance benefits.

California Senate Bill 1661: Paid Family Leave / Mandated Benefits

Purpose: To provide state disability insurance compensation for any individual who is unable to work due to the need to care for a seriously ill child, spouse, parent, or domestic partner, or for the birth, adoption, or foster care placement of a new child. Employees who are absent from work due to their own serious health conditions are already eligible for state disability insurance.

Effective date: The act becomes effective January 1, 2004. Benefits are payable for periods of family temporary disability leave commencing on or after July 1, 2004.

6 weeks wage replacement: Establishes, within the state disability insurance program, a family temporary disability insurance benefit program to provide up to 6 weeks of wage replacement benefits to workers who take time off work to care for a seriously ill child, spouse, parent, domestic partner, or to bond with a new child.

Employee contributions: Provides the benefits through additional employee disability insurance tax contributions.

Employer's right to require employee to use vacation leave: Authorizes employers to require that employees utilize up to 2 weeks of earned but unused vacation leave prior to that employee's receipt of these additional benefits, as provided.

Application to collective bargaining agreements: Specifies that these provisions may not be construed to relieve an employer of any collective bargaining duties.

National Labor Relations Board Will Oppose Enforcement of Employer "Neutrality" Law

(http://www.jacksonlewis.com/publications/newsletters/PS/2003/SU/01.cfm)

In a rare move, the National Labor Relations Board has authorized its General Counsel to take a position opposing the enforcement of certain provisions of California's so-called labor neutrality statute. General Counsel Arthur F. Rosenfeld will formulate the arguments and file a "friend of the court" brief on the NLRB's behalf in the litigation pending before the U. S. Court of Appeals for the Ninth Circuit. The Board will oppose the statute on the grounds that the provisions prohibiting California employers from using state funds to assist, promote or deter union organizing are preempted by the National Labor Relations Act and are invalid. [*Chamber of Commerce of the United States v. Lockyer*, Nos. 03-55163 and 03-55169 (9th Cir. 2003).]

Attorneys representing the parties in the litigation presented their arguments on May 27 in a closed door proceeding with all five members of the Labor Board, as well as the General Counsel and a number of agency staff. In separate sessions, representatives from the Chamber of Commerce of the United States and other plaintiffs in the case, the State of California, and the AFL-CIO argued for and against Board involvement in the litigation. Following the oral arguments, the Board voted 3-2 to authorize the General Counsel's intervention.

Bradley Kampas, a partner in the San Francisco office of Jackson Lewis, argued the matter on behalf of the plaintiff employer groups in the litigation, which include the Chamber of Commerce and the California Association of Health Facilities. "*It was a privilege to appear before the Board*," Mr. Kampas commented. "*It was obvious the members were very well prepared, asked excellent questions, and truly appreciated how significant this litigation is to the future administration of the NLRA*."

Legislation mandating employer silence in the face of union organizing attempts exists or has been introduced in at least nineteen other states, including Illinois, Massachusetts and Pennsylvania. Spearheaded by the AFL-CIO, the state "*neutrality*" bills are the focus of legislative and political initiatives to jump start organized labor's struggling organizing efforts

In 2002, the U. S. Chamber, CAHF, and other employer associations successfully argued their case before the U. S. District Court for the Northern District of California. They asserted that the state law and its companion bills are part of a state-by-state campaign by organized labor to modify the federal laws and dilute employer "*free speech*" rights under the NLRB.

Recent statistics show that unions win about 50% of the elections held. However, that number increases significantly when employers are bound by neutrality clauses, according to a 1999 AFL-CIO study showing a leap in that percentage to 84%. While voluntarily agreed to and collectively bargained neutrality clauses explicitly

incorporate the will of the parties into the labor/management relationship, state mandated neutrality provisions do not.

The effects of the California law, should it ultimately be upheld, will reach a large portion of the employer community. Many employers providing critical health care and social services in California are 100% dependent on state funds for revenues. Under the California law, these employers cannot use even the profits on their state contracts to express their views about unionization. Employers conducting business on state property are forbidden to talk to their employees about unions at the workplace. Federal law protecting the rights of employees to discuss their views on unions during working hours potentially are in conflict with the state law.

The California law presumes that employers co-mingle money received from state funding sources with other funds. To avoid any suggestions of impropriety or unlawful conduct, virtually every employer would be required to maintain dual accounting systems to show that no state funds were used to educate, train, or inform the workforce about either the pros or cons of union representation.

NATIONAL LABOR RELATIONS BOARD
(http://www.nlrb.gov/press/r2493.html)

OFFICE OF THE GENERAL COUNSEL

WASHINGTON, D.C. 20570

FOR IMMEDIATE RELEASE **(R-2493)**
Thursday, May 29, 2003 **202/273-1991**
www.nlrb.gov

LABOR BOARD AUTHORIZES ITS GENERAL COUNSEL TO PROCEED ON HIS RECOMMENDATION TO TAKE POSITION IN NINTH CIRCUIT CASE THAT TWO PROVISIONS OF CALIFORNIA STATUTE ARE PREEMPTED BY NLRA

The National Labor Relations Board announced today that it voted 3-2 (Chairman Battista and Members Schaumber and Acosta; Members Liebman and Walsh dissenting) to authorize its General Counsel to proceed on his recommendation to take the position, in federal court, that certain provisions of a California statute, Calif. Gov. Code §§ 16645.2 and 16645.7, are preempted by the National Labor Relations Act and are, therefore, invalid. The provisions of the state statute prohibit employers from using state funds to assist, promote or deter union organizing. Although the Board authorized its General Counsel to proceed, it left to him the discretion to formulate and express the arguments to be made against the California law. The case is *The Chamber of Commerce of the U.S. v. Lockyer,* 225 F. Supp 2d 1199 (C.D. Cal. 2002), pending appeal (9th Cir. 03-55169, 03-55166).

HHS Guidance Summarizes HIPAA Privacy Compliance Requirements

(http://www.jacksonlewis.com/publications/newsletters/PS/2003/WI/02.cfm)

In December 2002, the Department of Health and Human Services issued a compilation of new and existing guidance about key elements of the requirements of the Health Insurance Portability and Accountability Act of 1996, *Standards for Privacy of Individually Identifiable Health Information* (Privacy Rule). The HHS guidance preceded the April 14, 2003 (April 14, 2004 for small health plans) deadline for compliance with the "Privacy Rule."

What is the HIPAA Privacy Rule?

The HIPAA Privacy Rule generally prevents the disclosure of *protected health information (PHI) by covered entities* (which includes most group health plans and health care providers) to non-covered entities without authorization from the subject of the PHI (i.e., the patient). To comply with these requirements, covered entities must implement policies and standards to protect and guard against the misuse of PHI. Failure to timely implement these policies and standards may, under certain circumstances, trigger the imposition of civil or criminal penalties.

Are employers subject to the HIPAA Privacy Rule?

The Privacy Rule applies to *covered entities*. Since HIPAA does not give HHS the authority to regulate private businesses, employers and other plan sponsors are technically not "covered entities" subject to the Privacy Rule solely by virtue of acting as a plan sponsor and offering benefit plans to their employees. Nonetheless, plan sponsors that either require access to PHI to carry out administrative functions or that become involved in the administration and operation of a group health plan will have to comply with the HIPAA Privacy Rule on behalf of their group health plans.

What group health plans are subject to the HIPAA Privacy Rule?

HIPAA applies to any group health plan that has more than 50 participants or that is administered by an entity other than the plan sponsor. The only group health plans not subject to the Privacy Rule are plans administered by the plan sponsor with fewer than 50 participants.

Does the size of my group health plan matter?

Yes, the size of the plan affects the compliance deadline. HIPAA distinguishes between group health plans and small health plans. A small health plan is defined as a plan with less than $5 million dollars of annual receipts. Annual receipts are measured by premiums (for an insured plan) or contributions (for a self-insured plan). The compliance deadline for small health plans is April 14, 2004.

Does it matter if our plan is insured or self-insured?

Yes. Fully-insured plans that do not engage in administrative activities and that do not receive PHI generally have a minimal compliance burden. Self-insured plans, however, are presumed to receive PHI and will have a significant compliance burden.

How are my company's HIPAA compliance obligations determined?

If your company is a health care provider or clearinghouse, it is a covered entity subject to the myriad of HIPAA compliance requirements.

If your company is not a health care provider or clearinghouse, is not involved in claims processing or other plan administrative activity, and does not receive PHI, your health insurer or HMO may bear the brunt of the compliance burden.

Does the Privacy Rule apply to our health FSA?

Yes, it does. Although HHS has been asked to exempt health flexible spending arrangements (FSA) from the Privacy Rule, it has not yet done so. Accordingly, under current law health FSA's are group health plans covered by HIPAA. Further, health FSA's are almost always self-insured. Therefore, if your health FSA is administered 'in-house' and has 50 or more participants, it is a covered entity under the Privacy Rule, even if all of your other group health plans are fully-insured.

What can we do to avoid having our health FSA treated as a covered entity?

One possible solution would be to 'outsource' the administration of the health FSA. This could take the FSA out of HIPAA's definition of group health plan. Another, albeit temporary, solution would be treat the FSA as a separate plan. This would take advantage of the delayed compliance date if the health FSA would qualify as a small health plan. This strategy may also be advantageous as HIPAA regulators are believed to be reviewing the status of FSA's and may issue guidance in the future.

Are all employee medical records PHI?

No, some medical records are considered "employment records" which are exempt from the Privacy Rule. In determining what medical information is PHI, the focus should be on the basis for obtaining the information, not the nature of the information. In this regard, information obtained by a company in its role as 'employer' is generally not considered PHI. For example, if an employee submits medical records for the purpose of FMLA leave certification or workers' compensation benefits, those records are employment records, not PHI. Please note, however, that employment records may be subject to other laws regarding use and disclosure.

To what extent, if any, does compliance with the Privacy Rule require significant restructuring, such as redesigning office space or upgrading computer systems?

The Privacy Rule generally requires that covered entities take reasonable steps to limit the use or disclosure of PHI to the minimum necessary to accomplish the intended purpose. This includes making reasonable efforts to limit access to PHI to those in the workforce that need access based on their roles in the covered entity. Based on this reasonableness standard, HHS does not consider facility redesigns as necessary to meet the reasonableness standard for minimum necessary uses.

However, covered entities may need to make certain adjustments to their facilities to minimize access, such as isolating and locking file cabinets or records rooms, or providing additional security, such as passwords, on computers maintaining personal information. The steps a company takes in this regard may depend on the nature and size of the organization.

For access to the text of the Privacy Rule, go to the Department of Health and Human Services website: http://www.os.dhhs.gov/ocr/hipaa/finalreg.html.

HIPAA Privacy Rule Impacts Employer Drug Testing Procedures

(http://www.jacksonlewis.com/publications/articles/20030331/default.cfm)

The new Health Insurance Portability and Accountability Act rule on privacy scheduled to go into effect on April 14 may reach as far as the disclosure of information about workplace drug testing and substance abuse management. The *Standards for Privacy of Individually Identifiable Health Information*, known as the Privacy Rule, generally will prevent "covered entities" from disclosing protected health information to non-covered entities without authorization from the subject of the protected health information. The disclosure requirements may apply to many collection facilities, laboratories, Medical Review Officers and other service providers who analyze and review applicants' and employees' drug and alcohol test results.

"Covered entities" under HIPAA must require employers using their services to provide HIPAA-compliant authorization before releasing drug and alcohol test results (*i.e.*, protected health information) for employees and job applicants. Forms currently being used by employers for this purpose may not meet the requirements of the regulations which identify the key components and specifics for the authorization form. Additionally, the forms must be signed by the employees or applicants. As a practical matter, since HIPAA compliance ultimately falls on the shoulders of the "covered entity," the collection facility, laboratory or Medical Review Officer may have its own authorization form for employers.

In addition to the release of test results, other aspects of an employer's substance abuse policy may require use of a HIPAA-compliant authorization form. For example, when an employee enters into substance abuse rehabilitation, an employer may require progress reports from the substance abuse professional who evaluated and treated the employee. If the substance abuse professional is a "covered entity" under HIPAA, the employer may then be required to have the employee sign a specific HIPAA-compliant authorization form permitting the release of the "personal health information", *i.e.*, the substance abuse professional's records, to the employer.

Employers also should be aware that this federal law does not preempt more stringent state law requirements, where applicable.

ACCA's 2003 Annual Meeting
Charting a New Course

Employment Law Year in Review:

Finding Fair Winds in a Sea of New Workplace Laws and Regulations

Michael J. Lotito, Esq.
Jackson Lewis LLP

Legislative and Regulatory Update 2002 -- 2003

- Department of Labor's proposed FLSA regulations for "white collar" exemptions
- OSHA enhanced enforcement initiatives
- Federal family leave modifications and CA paid leave
- NLRB preemption of state "neutrality" laws
- HIPAA HIPAA Hooray ... I don't have to talk about it

A Facelift for the FLSA

On March 31, 2003, the U.S. Department of Labor proposed changes to the overtime pay exemptions under the Fair Labor Standards Act for executive, administrative, professional, outside sales and computer employees – the "white collar" exemption.

DOL Claims the Proposed Changes Will:

- Automatically guarantee overtime for an additional 1.3 million "low wage" workers;
- Strengthen overtime protections for an additional 10.7 million hourly workers;
- Enhance economic growth by reducing red-tape and litigation costs;
- Bring the overtime rules into the 21st century and help to clarify the rights of employees and employers.

Why the Proposed Revisions

- The current regulations are outdated:

  The duties test for the "core" white collar exemptions where last changed in 1949;
  - *The current salary levels of $155 or $250 per week are too low;*
  - *The salary levels have not been changed since 1975; and*
  - *The "salary basis" test has not been changed since 1954.*
- Business groups have clamored for change in response to the dramatic increase in wage-hour collective actions and multi-million dollar settlements.

Since Then…

- AFL-CIO claims 8M employees will lose overtime
- Over 78,000 comments received
  - Many from AFL-CIO
  - 1,900 from SHRM Grassroots
  - ACCA comments on behalf of Committee
- DOL said 1,100 were substantive
- July – House of Representatives against withholding funding to DOL for finalization of regulations
- But…

The Senate...

- On September 10 voted 54-45 to Withhold Funding

The House...

- On October 2 voted 221-203 as a non-binding motion, to instruct conference committee members to adopt Senator Harkin's position.

The Administration…

- Is not backing away
- President threatening a veto

Where are we really?

- Representative Regula (R) said DOL could raise salary threshold under the motion.
- Senator Gregg (R) - Chair of Senate Committee.
  - Will be Omnibus spending bill
  - Put in a higher salary test
  - The veto threat makes Senator Haskin's Amendment a "Point Pill"
  - Who is going to blink?
- And what is the fight about?

Summary of Changes

- Increase the salary levels test from $155.00 to $425.00 per week.
- Eliminate the "long" and "short" salary level and duties tests.
- Modify the duties test for executive employees.
- Modify the duties test for administrative employees.

Summary, cont.

_ Modify the duties test for professional employees.
_ Reorganize and consolidate the regulations for computer employees.
_ Eliminate the 20% restriction on non-exempt work for outside sales employees.
_ Create a "super salary" test for executive, administrative or professional employees who receive guaranteed annual compensation of at least $65,000.

Summary, cont.

- Modify the "salary basis" requirement to allow employers to take deductions for full day disciplinary suspensions for violations of workplace rules, such as sexual harassment policies.

- Modify the "window of correction" procedure so that employers who have a "pattern and practice" of non-compliance will lose an otherwise valid exemption.

Salary Level Increase

- Minimum salary for executive, administrative, professional and computer exemptions is $425.00.
- DOL selected the new salary based upon BLS 2000 current population survey.
- Based on BLS survey, 20% of salaried employees will fall below minimum salary and qualify for overtime.
- DOL estimates new salary levels will result in overtime for an additional 1.3 million employees.

Proposal for Office or Non-manual Workwork

- Tax
- Finance
- Accounting
- Auditing
- Quality Control
- Purchasing
- Procurement
- Advertising
- Marketing
- Research
- Safety and Health
- Personnel management
- Human Resources
- Employee Benefits
- Labor Relations
- Public Relations
- Government Relations

Criteria for "Position of Responsibility"

Work of substantial importance; or

Requiring a high level of skill.

Work of "Substantial" Importance Affecting General Business Operations or Finances:

- Providing consultant or expert advice to management.
- Making or recommending decisions that have a substantial impact on general business operations or finances.
- Formulating, interpreting or implementing management policies.

Examples, cont.

- Analyzing and recommending changes to operating practices.
- Planning long and short term business objectives.
- Analyzing data, drawing conclusions and recommending changes.
- Handling complaints, arbitrating disputes or resolving grievances.
- Representing the employer during important contract negotiations.

Work Requiring High Level of Skill or Knowledge:

- Specialized knowledge
- Abilities
- Advanced instruction

  Under the proposed rules, knowledge or abilities can be acquired through academic instruction or the equivalent advanced on-the- job training.

"Learned Employee" – Advanced Knowledge

Employees can acquire through a combination of:

- *Formal college level education*
- *Training*
- *Work experience*

Under current regulations work experience usually could not satisfy advanced knowledge requirement.

"Super Salary" Test

To meet this test, the employee must:

- perform office or non-manual work.
- be guaranteed total compensation of at least $65,000 per year.
- perform one or more duties of an executive, administrative or professional employee.

"Super Salary" Test, con't.

- does not apply to computer exemption;
- may count base salary, commissions and non discretionary compensation toward $65,000 requirement;
- may pro rate earnings for partial year employee. Earnings should be prorated by number of weeks employed.

Salary Basis Requirement

Employer can lose exemption if it engages in a pattern or practice of improper deductions for:

_ partial day absences for personal reasons or sickness or disability (non-FMLA absences);

_ full day absences for jury duty, attendance as a witness, or employer operating requirements, if any work performed in the same workweek.

Proper Deductions

Deductions from salary can be made for:

- full day absences for personal reasons, or sickness or disability, if the employer has a policy that provides compensation for salary loss;
- good faith penalties for infractions of safety rules of major significance (i.e., rules that prevent serious dangers in the workplace.)

Impact of Improper Deductions

If the employer has a "pattern or practice" of making improper deductions, the exemption will be lost:

- during the time period in which improper deductions were made.
- for any employees in the same job classification who worked for the managers responsible for the improper deductions.

Safe Harbor Rule

Exemptions will not be lost for improper deductions if the employer:

- implements and enforces written policy prohibiting improper deductions.
- notifies employees of the policy.
- reimburses employees for any improper deductions.
- does not repeatedly or willfully violate its policy or continue to make improper deductions.

OSHA's New Enforcement Initiatives

The Occupational Safety and Health Administration announced in March a new enforcement policy targeting 10,000 specific employers:

_ more robust workplace inspections;

_ heavy citations;

_ expanded penalties;

_ continuing governmental scrutiny.

OSHA Site Specific Targeting Program (SST)

- Identified establishments will be assigned a high priority for inspection in 2003 and early 2004.
- If a "high gravity" violation is identified in the course of an SST inspection at one establishment, *all other establishments under the same corporate identity* will be placed on the *primary* SST inspection list for this same year.

Substantial Punitive Consequences Under New OSHA Enforcement Initiative

- Tougher settlement provisions
- Automatic follow-up inspections
- Adverse publicity for employers
- Other consequences: pressure from unions and disgruntled employees; costs from additional assessed penalties; indirect costs from disruption caused by inspections

  Employers should determine whether any establishments are on the OSHA list; if so, prepare for the imminent inspection.

California Paid Family Leave: Mandated Benefits

_ Provides disability compensation for any individual who is unable to work due to the employee's own sickness or injury, the sickness or injury of a family member, or the birth, adoption, or foster care placement of a new child.

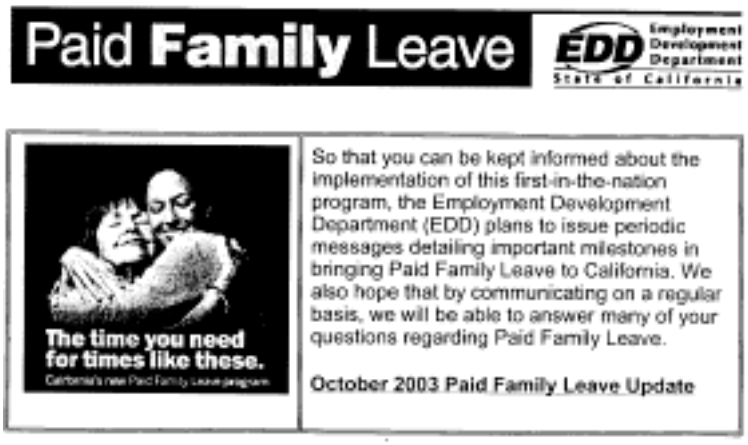
_ Expands state disability insurance coverage to provide benefits to employees who take time off to care for a covered family member or bond with a new or adopted child under the California Family Rights Act.

Six Weeks of Wage Replacement

- Establishes a family temporary disability insurance program to provide up to 6 weeks of wage replacement benefits.
- Provides additional benefits through employee contributions.
- Benefits payable for family temporary disability leaves that begin on and after July 1, 2004.

What California Employers Can and Should Do

- Employers can require employees to use up to two weeks of vacation leave.
- Employers who secure separate disability insurance should coordinate with their providers to ensure proper coverage.



Outside California, Who Cares?

- Employers with multi-state operations
- Employers watching trends in CA and elsewhere
- Employers in states that have expanded family leave provisions beyond federal FMLA
- Employers in states with Democrat-controlled legislatures and…
- Modifications to FMLA after DOL finished with FLSA – the next battle

NLRB Intervention in State Mandated Employer Neutrality Law

- California law prohibits use of state funds for any purpose touching union organizing
- Forces discrete accounting system for state funds versus other income and outgo
- Prohibition includes employee training
- US Chamber challenge pending at 9th Circuit with NLRB opposing state law
- Other states already have or are considering similar prohibitions

And

October 6, DOL released final regulations raising Union financial reporting under LMRDA

Gray Davis signs S.B. 2 regarding mandated health care

- By January 1, 2006, employers with more than 200 workers must provide health coverage for employees and their dependents
- By January 1, 2007, employers with 50 to 199 employees must provide coverage to employees only
- Employees must work at least 100 hours a month for at least three months for the same employer to be eligible and contribute up to 20% of the premium cost
- ERISA Preemption????

HIPAA, HIPAA, Hooray

I don't have to talk about HIPAA ...

See course materials this session for information on HIPAA "Privacy Rule"

See course materials for Session 206,
"HIPAA HIPAA Hooray, So You're Compliant but Now What?"

EMPLOYEE BENEFITS – YEAR IN REVIEW

a/k/a

"A Year of Change: Employer Stock, Health Care Decision Making, and Defined Benefit Plan Funding"

Dana M. Muir
Louis and Myrtle Moskowitz Research Professor of Business and Law and
Associate Professor of Business Law
University of Michigan Business School

 I am grateful for the research assistance of R. Joshua Ruland, who did a great deal of the summarizing for this article. I also appreciate the research support provided by the University of Michigan Business School.

I. INTRODUCTION

The Supreme Court, Department of Labor (DOL), and Internal Revenue Service (IRS) all took a number of significant actions in the employee benefits arena during late 2002 and the first part of 2003. The federal courts issued many decisions of interest during the same time period. While not yet decided, the Enron litigation is interesting both from the perspective of the suit filed by private plaintiffs, but more importantly given the time period covered by this paper because of the suit filed by the DOL during June 2003. Important legislation is pending in Congress as this paper is being written in mid-July 2003.

II. SUPREME COURT

The Supreme Court decided two ERISA cases during its 2002-2003 term: *Kentucky Assn. of Health Plans, Inc. v. Miller*, 123 S. Ct. 1471 (2003) and The *Black & Decker Disability Plan v. Nord*, 123 S. Ct. 1965 (2003).

A. Decisions by the Supreme Court During the 2002-2003 Term.

1. *Kentucky Assn. of Health Plans, Inc. v. Miller*, 123 S. Ct. 1471 (2003).

A number of HMOs and an HMO association argued that ERISA preempts Kentucky's all willing provider law. The district court concluded that ERISA's savings provision saved the Kentucky statute from preemption and the Sixth Circuit affirmed. The Supreme Court affirmed in a decision that is notable both because of its specific import for state all willing provider laws and because of its rejection of the traditional McCarran-Ferguson analysis for analyzing what constitutes "insurance" for purposes of ERISA's savings clause.

Kentucky law contains both a general all willing provider provision and language permitting chiropractors to participate as primary chiropratic providers. 123 S. Ct. at 1473-74. Petitioners challenged the Kentucky statute as being preempted by ERISA because it interferred with their cost containment and quality control efforts. Those efforts relied in part on the HMOs' ability to limit the providers in their networks. *See id.* at 1474.

Both the district court and the Sixth Circuit determined that the Kentucky law would be preempted as a law that "relate[s] to an employee benefit plan" unless it falls within ERISA's savings clause. 227 F.3d 352, 363 (6th Cir. 2000); 14 F. Supp. 2d 991, 1000-01 (1998). The Supreme Court granted certiorari on and confined its analysis to the second prong of this analysis – whether the Kentucky provisions are "'laws… which regulate insurance'" for purposes of ERISA's savings clause. 123 S. Ct. at 1475.

The surprise in the Court's decision was its decision to "make a clean break from the McCarran-Ferguson factors…" *Id.* at 1479. The Court stated the new two-part test for laws that are saved as: ""First, the state law must be specifically directed toward entities engaged in insurance. . . . Second, . . . the state law must substantially affect the risk pooling arrangement between the insurer and the insured." *Id.*

In application, the Court determined that the Kentucky laws were directed at entities engaged in insurance because they applied only to situations involving health insurers and health benefit plans. *Id*. at 1475. The fact that the laws incidentally prevented Kentucky physicians from forming exclusive networks did not mean the laws were not directed at insurers. *Id.* at 1475-76. Similarly, the Court found that the Kentucky laws regulate an insurance practice because they "impos[e] conditions on the right to engage in the business of insurance" even though they may not regulate "the business of insurance" as defined in the McCarren-Ferguson Act. *Id.* at 1476-77. Finally, the Kentucky laws substantially affect the type of risk pooling arrangements offered in Kentucky because insureds have no ability to seek to limit premiums in exchange an exclusiver provider network. *Id.* at 1477-78.

2. *The Black & Decker Disability Plan v. Nord*, 123 S. Ct. 1965 (2003).

Social Security regulations provide that a treating physician's opinion be given special weight when deciding an individual's entitlement to Social Security benefits. This has come to be known as the "treating physician rule." The Ninth Circuit decided that the rule should be used in ERISA disability cases where a plan administrator questioned a participant's or beneficiary's right to benefits. 123 S. Ct. at 1969. In an unanimous opinion, the Supreme Court rejected the mandatory use of the treating physician rule in ERISA disability cases. 123 S. Ct. at 1967.

Mr. Nord had been been treated by two physicians who certified his disability. The plan arranged for an independent examination and that physician concluded that Mr. Nord was not totally disabled. The plan administrator, Black & Decker, then denied his disability claim on the basis of the independent examination. The district court upheld the plan administrator's decision under an abuse of discretion standard. *Id.* The Ninth Circuit not only reversed, but also granted summary judgment to Mr. Nord, deciding that where the treating physician and the plan's clinical examiner disagree on the extent of disability, the treating physician rule permits a plan administrator operating under a conflict of interest to reject the treating physician's conclusions only if the administrator "gives 'specific, legitimate reasons for doing so that are based on substantial evidence in the record.'" 296 F.3d 823, 831 (9th Cir. 2002) (citations omitted).

The circuits had split on the appropriate use of the treating physician rule. The Third and Ninth Circuits favored some use of the rule. *Jebian v. Hewlett-Packard Co. Employee Benefits Org. Income Prot. Plan*, 310 F.3d 1173 (9th Cir. 2002); *Sketvedt v. E.I. DuPont Nemours & Co,* 268 F.3d 167, 184, 26 EB Cases 2610 (3d Cir. 2001); *Regula v. Family Care Disability Survivorship Plan*, 266 F.3d 1130 (9th Cir. 2001). Other circuits either expressed skepticism or rejected use of the rule for ERISA cases. *Tickle v. Long Term Disability Plan of Marathon Ashland Petroleum, LLC,* No. 01-2100, 2002 U.S. App. LEXIS 9058, at *9 (4th Cir. May 10, 2002); *Leahy v. Raytheon Co.*, 315 F.3d 11, 21 n.8 (1st Cir. 2002); *Turner v. Delta Family-Care Disab. & Survivorship Plan*, 291 F.3d 1270, 1274 (11th Cir. 2002); *Salley v. E.I. DuPont de Nemours & Co*., 966 F.2d 1011, 1016, 15 EB Cases 2057 (5th Cir. 1992); *Jett v. Blue Cross & Blue Shield of Ala*., 890 F.2d 1137, 1140, 11 EB Cases 2433 (11th Cir. 1989).

In resolving this split among the circuits, the Supreme Court reasoned that nothing in ERISA or in DOL regulations or guidance called for special deference to the conclusions of treating physicians. 123 S. Ct. 1970. The adoption of a treating

physician rule for ERISA cases would require resolution of whether treating physicians' opinions are more credible than other evidence and whether differences between the Social Security disability program and ERISA plans should affect the rule for ERISA cases – resolutions the courts "are ill equipped" to make. *Id.* at 1971. The Court did say, however, that "Plan administrators, of course, may not arbitrarily refuse to credit a claimant's reliable evidence, including the opinions of a treating physician." *Id.* at 1972.

B. Grants of Certiorari for the Supreme Court's 2003-2004 Term.

1. *Yates v. Henton*, 287 F.3d 521 (6th Cir. 2002), *cert. granted,* 123 S. Ct. 2637 (2003).

The question of whether a worker-owner may be classified as an ERISA participant under section 3(7) has split the circuits. While the First and Sixth Circuits have ruled that sole shareholders may not be participants (see *Kwatcher v. Massachusetts Serv. Employees Pension Fund,* 879 F.2d 957 (1st Cir. 1989); *Agrawal v. Paul Revere Life Ins. Co.,* 205 F.3d 297 (6th Cir. 2000)), the Fourth and Fifth Circuits have ruled that sole shareholders may be participants. (See *Madonia v. Blue Cross & Blue Shield,* 11 F.3d 444 (4th Cir. 1993); *Vega v. National Life Ins. Servs., Inc.,* 188 F.3d 287 (5th Cir. 1999)). The Supreme Court has granted certiorari on this issue in *Yates v. Henton*.

Yates, an M.D., owned a corporation known as Raymond B. Yates, M.D., P.C. that maintained a profit sharing pension plan covering four people including Dr. Yates, who was also the plan administrator and trustee. Dr. Yates took a $20,000 loan from the plan and later repaid the loan in full, with accumulated interest, three weeks before an involuntary bankruptcy petition was filed against him. The plan document made provision for these types of participant loans. The trustee in bankruptcy filed suit against the plan, and Dr. Yates as plan trustee, to recover the loan repayment. Dr. Yates claimed exemption on the grounds that applicable nonbankruptcy law, ERISA, allows, and in fact requires, that an anti-alienability clause govern the plan. 287 F.3d at 524-25.

While the Sixth Circuit recognized that the exemption would allow the plan to retain the repayment if the exemption were exercised by a participant, the court ruled that Yates was a sole owner and employer and therefore was not a participant. *Id.* at 525. The Supreme Court granted certiorari to decide the question of whether an owner/employer can also be a participant under ERISA.

2. *Cline v. General Dynamics*, 296 F.3d 466 (6th Cir. 2002), *cert. granted,* 123 S. Ct. 1786 (2003).

The question addressed by Cline is whether the Age Discrimination in Employment Act (ADEA), 29 U.S.C. §§ 621-634, prohibits the practice of discriminating against younger employees that fall within the protected class (workers over the age of 40); the so called practice of "reverse discrimination." The Sixth Circuit ruled that it did, but that ruling is in direct opposition to decisions the First and Seventh Circuits. The Sixth Circuit, acknowledged the views of its sister circuits, but stated that: "for a variety of reasons, however, we do not find the reasoning undergirding these opinions persuasive." 296 F.3d at 470. Instead, the Sixth Circuit believed that: "Congress has singled out the over-40 class of workers from the general workforce for protection from age

discrimination by their employers." *Id.* at 471. And: "An action is either discriminatory or it is not discriminatory, and some discriminatory actions are prohibited by law." *Id*. The Court said that the "plain meaning of the statute precluded any other approach." *Id.* at 470.

General Dynamics engaged in collective bargaining with its employees union, the United Auto Workers, and reached an agreement that did not include retirement health insurance - a benefit that retirees had been entitled to before the new agreement after reaching the age of 50 and 30 years of seniority. The agreement excepted those employees already entitled to those benefits. That is, employees who had 30 years of seniority and were over the age of 50 on July 1, 1997 were still entitled to the benefits the old contract had stipulated. *Id.* at 467-68.

A class of employees between the ages of 40 and 49 filed a complaint in federal court claiming they were being discriminated against on the basis of age. The district court dismissed their complaint on the basis that ADEA does not prohibit reverse discrimination. *Id.* at 468. The Sixth Circuit reversed and ruled that ADEA provided protection from reverse discrimination as it was simply another form of discrimination. The court acknowledged that the case presented unusual facts because, unlike typial ADEA suits, the plaintiffs were younger than the preferred individuals, but said that the terms of the statute extended protection to plaintiffs. *Id.* at 472.

III. LOWER COURT DECISIONS

A. Preemption.

1. *Arana v. Ochsner Health Plan*, No. 01-309222003, U.S. App. LEXIS 13918 (5th Cir. July 10, 2003) (*en banc*).

Ochsner Health Plan (OHP) paid health care benefits on behalf of Arana for injuries Arana suffered in an automobile accident. Arana later filed tort claims associated with the accident and then settled with multiple insurance companies. OHP sought, based on a plan subrogation provision, to recover the amounts Arana received in settlement from the other insurers. 2003 U.S. App. LEXIS 13918, at *2-3.

Arana sought, based upon a state law that allegedly precludes subrogation, a declaratory judgment in Louisiana state court that he had no obligation to repay OHP. An Eighth Circuit panel decided that ERISA did not preempt Arana's declaratory judgment action. The Eighth Circuit granted en banc review and in a unanimous decision determined that ERISA section 502(a)(1)(B) completely preempted Arana's state law action. *Id.* at *10. The court indicated that Arana's claim could be characterized as one either to enforce his rights to benefits under the plan or, using a more complex analysis, as one for benefits due. *Id.* at *10-11.

One interesting aspect of the en banc opinion is the court's use of the plan's choice of law provision. The court observed that the Louisiana law became part of the plan "because the plan explicitly provides that the plan is to be enforced according to Louisiana law." *Id.* at *12. To my knowledge this is an

approach that has not been used before by any federal court in the ERISA context and was suggested in the amicus brief I co-authored with Professor Ed Cooper at the request of the court. Plan sponsors should review their plans for boilerplate choice of law provisions and consider the implications if state law is built into the plan through those provisions.

2. *James v. Pirelli Armstrong Tire Corp.,* 305 F.3d 439, 2002 U.S. App. LEXIS 19071 (6th Cir. 2002).

While downsizing, Pirelli Armstrong Tire Corporation (Pirelli) held mandatory sessions that included information on the status of health care benefits in retirement. Specifically, a scripted speech was given, in addition to a slide presentation, and recorded audio presentation that informed employees that their health care benefits would not change if they retired immediately, but would become less favorable if they remained with the company for several more years. Human Resources liaison, Shirley Pike, gave the slide presentation and answered questions both at the meetings and in private. According to the court, "Pike ... informed employees that their benefits would remain unchanged during their lifetimes. When employees asked Pike about language in the [Summary Plan Description] that allowed the company to alter or amend the plan, Pike stated that it ... enable[d] the company to change insurance carriers." 2002 U.S. App. LEXIS 19071, at *7-8. "Pike added that to the best of her knowledge, the company provided her with truthful and accurate information to present to the employees and the plan beneficiaries, and that the company advised her to answer questions posed by employees about the benefits so as not to mislead them." *Id.* at *8. Plaintiff retirees filed suit when their coverage was changed, resulting in increased out-of-pocket health care expenditures. *Id.* at *9.

The court decided that, although the provision of inaccurate information was unintentional, Pirelli still breached its fiduciary duty and was liable for the damage incurred. To win a fiduciary duty claim, the court opined that: "a plaintiff must show: (1) that the defendant was acting in a fiduciary capacity when it made the challenged representations; (2) that these constituted material misrepresentations; and (3) that the plaintiff relied on those misrepresentations to their (sic) detriment." *Id.* at *23. The Sixth Circuit distinguished it's earlier decision in *Sprague v. General Motors*, 133 F.3d 388 (6th Cir. 1998) (*en banc*) in which "GM ... did not tell the early retirees at every possible opportunity that which it had told them many times before -- namely that their benefits were subject to change." *Id.* at *28. In contrast, in Pirelli, there was a consistent message that the benefits would not change.

3. *Cicio v. Does,* 321 F.3d 83 (2nd Cir. 2003).

The *Cicio* court delved into the intersection between state malpractice law and ERISA's regulation of health care plans. In so doing, it drew a fine distinction between coverage and care. The dichotomy between these two is founded upon the ideas of "eligibility" and "treatment" decisions. The court noted the reduction of the gap between narrowly defined contract interpretation in the first and the question of the second: " 'Given a patient's constellation of symptoms, what is the appropriate medical response?' [E]ven if a physician does not control, direct, or influence a plaintiff's treatment, and even if the sole consequence of a physician's decision is reimbursement or its denial, that decision may nonetheless be a mixed eligibility and treatment decision." 321 F.3d at 102 (internal citations omitted).

Bonnie Cicio, wife of decedent Carmine, filed state law claims, including malpractice, against the defendants after her husband was denied approval for desired treatment for a blood cancer, multiple myeloma. Several letters were exchanged between Cicio's treating physician, Dr. Samuel, and the insurer's utilization review physician, Dr. Spear. In the exchange, Spear rejected a proposed treatment, recommended by Samuel, but approved another that was not suggested by Samuel.

ERISA preempted all of the state law claims except malpractice. The court determined "that a state law malpractice action, if based on a 'mixed eligibility and treatment decision,' is not subject to ERISA preemption when that state law cause of action challenges an allegedly flawed medical judgment as applied to a particular patient's symptoms." *Id* at 102. Further, the court stated that "Dr. Spears apparently made a patient -specific prescription of appropriate treatment by denying one treatment and authorizing another that Dr. Samuel had not requested." *Id.* at 104.

4. *Trustees of the AFTRA Health Fund v. Biondi* 303 F.3d 765 (7th Cir. 2002).

Richard Biondi's divorce agreement stipulated that he would pay the COBRA transition payments from his medical insurance for two years following his divorce. Rather than make these payments, he instead neglected to inform his employer or the plan of his divorce at all. During the next five years, Biondi's ex-wife billed $122,792.86 in medical expenses to the insurer. When the plan discovered the divorce, it filed suit to recover the medical payments, expenses associated with the lawsuit, and $50,000 in damages under ERISA and Illinois state fraud law. The Seventh Circuit ruled that Illinois state fraud law was not preempted by ERISA. 303 F.3d at 769.

The Court began by noting that, "the Trustees' claim is for common law fraud, a traditional area of state regulation," and that as such, there is a "starting presumption that Congress does not intend to supplant state law." *Id.* at 775 (internal citations omitted). The argument made by the court was based on the intent of the statute and "the Trustees' [of the plan] claim [of fraud] does not threaten in any way Congress's goal of national uniformity." *Id* at 775. The claim certainly does not refer "to a claim where the state law at issue relied, for its very operation, on a direct and unequivocal nexus with ERISA plans." *Id* at 778. Rather, the reverse, that "the plan was only the context in which this garden variety fraud occurred." *Id.* at 780 (internal citations omitted). The court also was troubled by the fact that if ERISA had preempted the Illinois fraud law, "a plan participant [would be] entitled to 'blanket immunity' from damages under state tort law simply because he chose to defraud an employee benefit trust fund." *Id.* at 782. Therefore, the state law fraud claim was not preempted by ERISA.

B. Section 510.

1. *Milsap v. McDonnell Douglas,* unreported, summary based upon orders of July 14, 2003 and May 28, 2003.

Plant closings rarely result in damage recovery by employees under ERISA

section 510 because to do so requires plaintiffs to show specific intent. However, in *Milsap*, the class of former employees and McDonnel Douglas Corporation (MDC) settled for just that: $36 million in damages for discriminatory termination. In addition, the class has a potential upside in back-pay damages and no downside pending an inlocutory appeal decision by the Tenth Circuit.

The district court for the Northern District of Oklahoma approved a settlement that broke with the norm after several important findings. *Milsap* is only the third plant closing case to result in damages for the former employees. In the two previous cases, " 'smoking gun' documents were found as evidence of discriminatory intent." Order of May 28, 2003 (fees), at 17. However, "the Court [was] unable to give deference to a business decision when the evidence produced by the Defendant does not support the characterization of the decision as a 'business decision.'" *Id.* at 3. In addition, MDC was sanctioned for repeated discovery abuses including destruction of documents and material misstatements of fact. In light of the abuses and absent good cause to defer to the business judgment rule, the district court found that the evidence supported an inference "that the proffered reason was not the true reason for the employment decision" *Id.* at 3. and that MDC was liable for violation of ERISA. After discovery with regard to damages but before the damages trial could commence, the class and MDC reached this settlement.

While a rare damages case, the settlement is unique in other ways. First, it leaves the issue of back pay on the table. MDC contends that, as a matter of law, back pay does not constitute "equitable relief," as defined in *Great-West Life & Annuity Ins. Co. v. Knudson,* 534 U.S. 204 (2002). This issue was accepted as an interlocutory appeal by the Tenth Circuit. If back pay is not equitable relief, then the litigation will end. If, however, back pay is equitable relief, the damages case will reopen on that point. In addition, the settlement both distributes the settlement damages in a novel manner, reflecting the loss of the class members rather than pro rata, and allows a mechanism for class members to appeal their position in the class to both the class attorneys and a federal magistrate. Order of May 28, 2003 (fees), at 7-9.

2. Lessard v. Applied Risk Management, 307 F.3d 1020 (9th Cir. 2002).

Professional Risk Management (PRM) purchased the assets of Applied Risk Management (ARM). The purchase agreement called for the transfer of all employees from ARM to PRM except for those who were not actively employed at ARM on the date of the sale and who did not fall within one of a few exceptions. The plaintiff, Denice Lessard, had been off work for a long period due to an injury covered by workers compensation though she had remained entiteld to coverage under ARM's health care plan. 307 F.3d at 1022-23. She lost that health care coverage when ARM terminated its health care plan and PRM did not transfer her to active employment. Lessard sued ARM and PRM alleging, among other things, a violation of ERISA § 510. *Id.* at 1023.

The Ninth Circuit noted that, in the absence of the asset sale, ARM would not have been able to directly or indirectly "terminate the benefits of a select group of employees – most of whom were high-rate users of the company's Plan – because those employees were on medical leave and to offer those employees reinstatement of benefits only on the condition that they return to work." *Id.* at 1025-26. Similarly, ARM and PRM together could not accomplish the same result

through the acquisition agreement. *Id.* The court rejected defendants' argument that section 510 does not protect against benefit terminations that are incident to a corporate business transaction. *Id.* at 1026. Relying on the Supreme Court's decision in *Inter-Modal Rail Employees Ass'n v. Atchison, Topeka & Santa Fe Ry. Co.,* 520 U.S. 510, 515 (1997), the court determined that no such exception to 510 exists when "an employer selects for presumptive termination and denial of benefits specifically those employees presently on medical or disablity leave." 307 F.3d at 1026.

C. Fiduciary Duty.

1. Employer Stock Cases.

Two district courts recently addressed issues alleging fiduciary breach associated with employer stock in 401(k) plans. In ***Kling v. Fidelity Management and Trust Co.,*** No. 01-CV-11939-MEL 2003 WL 21554070 (D. Mass. June 3, 2003), the district court denied summary judgment to the defendants in an action where the only a subset of the participants were damaged by the alleged breach.

Kling participated in an Employee Savings Plan that included a sock fund, an undiversified fund consisting mostly of his employer's, Harnischfeger Industries, common stock. Plaintiff alleges that Harnischfeger and Prudential, the plan trustee, violated their fiduciary duty in connection with that common stock. Central to ERISA's section 502(a)(2) enforcement scheme is the idea that recovery for breach of fiduciary duty can only inure to the plan as a whole. The district court agreed with Kling's assessment that "recovery can inure to the plan without being allocated to each and every participant." *Id.* at 2. Further, the court said that: "Kling does sue on behalf of the Plan, and thus meets the requirements of § 409 as interpreted by the Supreme Court in *Russell*. That the harm alleged did not affect every single participant does not alter this conclusion." *Id.* at 5.

In ***In re: Williams Companies ERISA Litigation,*** unpublised opinion (N. D. Okla. July 14, 2003), the district court denied a motion to dismiss allegations of breach of fiduciary duty against an Investment and Benefits Committee. Williams Companies common stock was an investment option under the company's employee benefit plan and declined dramatically in value. Plaintiffs alleged that the members of the committees "knew or should have known" information that the stock was inflated. The defendants contended that "they had no duty to disclose material non-public financial information and, in any event, any such disclosure would have constituted a violation of federal securities laws." Court Order of July 14, 2003, at 18. The court, however, concluded that "had the Investment Committee recommended removing Williams from the list of available investment options, based upon its alleged knowledge that Williams stock was wrongfully inflated, the damage alleged here would not have occurred. This power to prevent damage establishes that the Investment Committee's authority was sufficient to form the basis for fiduciary responsibility in this case." *Id.* at 22. The court did, however, dismiss the claims against the company and the board of directors. *Id.* at 15 & 17.

Similarly, in ***Crowley v. Corning, Inc.,*** 234 F. Supp. 2d 222 (W.D.N .Y. 2002), the plaintiff filed suit for breach of fiduciary duty with regard to Corning

stock held in the 401(k) plan and ESOP. The court dismissed the complaint for as to all defendants. Defendant Corning was found to not have fiduciary duty vis-a-vis the plan in regard to the employer stock decisions because those actions were taken as part of its settlor functions. Defendant board members were not alleged to have breached their fiduciary duty with regard to selecting or removing Investment Committee members, the only fiduciary duty they were found to have.

The plaintiff alleged that Investment Committee members breached their fiduciary duties but made "no specific allegation that the Committee members actually possessed the 'adverse information'" which might have triggered a fiduciary obligation to act in the best interest of the participants and beneficiaries. 234 F. Supp. 2d at 230. "Rather, plaintiff's allegations are made against all defendants, without specifying when the 'adverse information' was available, or known, to Committee members, or any single one of them." *Id.* That is, the district court held that the plaintiff had made only "conclusory allegations [that were] insufficient to show that following the ESOP portions of the Plan was imprudent under the circumstances" *Id.*

2. Chao v. Enron Corp., complaint filed June 26, 2003.

The Secretary of Labor has filed a complaint of breach of fiduciary duty against Enron Corp., its board of directors, CEOs Jeffrey Skilling and Kenneth Lay, its employee retirement plans' Administrative Committee members, and other individuals. Several issues will be important. Did the Administrative Committee's actions significantly diverge from the actions of a prudent person with like knowledge? Did the failure to inform the Committee of risks specific to individual business ventures constitute a breach of duty by Lay, Skilling, and Enron? Did the Board's failure to appoint a trustee violate its duty of care?

The Administrative Committee members are charged with violating their duties of prudence and loyalty, not abiding by the plan documents, and failing to act on information, both public and non-public, that would call into question the investment in Enron stock. Specifically, the allegations include assertions that the Committee did not adjust the level of investment the plans had in Enron stock despite warnings in the press of the potential dangers, they did not diversify the holdings of the plans, individual members - who had access to internal information - did not react to internal memos warning of the company's potential problems, nor did the Committee meet frequently or discuss when they did meet adjusting the level of investment before or during a rapid decline in the value of Enron stock. The Complaint alleges that: "At no time did any of the Committee Defendants take any action to effectively monitor...the Plans' investment in Enron stock." Complaint at 35.

Enron, Lay, and Skilling allegedly did not observe their fiduciary obligation to monitor the activities of the Administrative Committee nor did they properly appoint or remove members of the Committee. According to the Complaint: "At no time did Enron, Lay or Skilling prudently consider or review the performance of the Committee Defendants relating to the Plans' investments in Enron stock..." Complaint at 40. In addition, they had access to information that cast doubt on the virtue of investing in Enron stock and yet did not inform either the Administrative Committee or the employees who held stock in the plan. Finally, they did not correct misrepresentations made by Lay that encouraged plan participants to purchase Enron stock as it was still a good investment.

The board of directors had the fiduciary obligation to monitor the Administrative Committee with the appointment of a trustee as stated in the plan documents. Allegedly, the board did not appoint a trustee nor did they take steps to monitor the Committee in other ways to fulfill their obligation. By doing so, the Complaint asserts that the Board, "caused the [Plan] to suffer losses which it would not have suffered." Complaint at 44.

The Department's complaint asks that the Administrative Committee, Lay, Skilling, Enron, and the board of directors be held personally liable to the plan participants for losses and that they be enjoined from holding fiduciary positions in the future.

D. Health Care Plans – Standard of Review, etc.

Three circuits have adopted the position that if a plan fails to conduct an appeal in an appropriate and timely manner, the plan forfeits the discretionary review to which it otherwise would be entitled.

In the most recently decided case, ***Seman v. FMC Corp.Retirement Plan for Hourly Employees,*** 2003 U.S. App. LEXIS 13280 (8th Cir. July 1, 2003), the Eighth Circuit ruled that an employee whose denial of benefits appeal had not been resolved in a reasonable amount of time could be entitled to a de novo review. The court opined, " When a plan administrator denies a participant's initial application for benefits and the review panel fails to act on the participant's properly filed appeal, the administrator's decision is subject to judicial review, and the standard of review will be de novo rather than for abuse of discretion if the review panel's inaction raises serious doubts about the administrator's decision." *Id*. at 14. Seman raised "serious doubts" here by filing many documents in addition to those filed with his initial application.

In ***Gilbertson v. Allied Signal, Inc.,*** 328 F.3d 625 (10th Cir. 2003), the Tenth Circuit went further, stating that, "when the administrator fails to exercise his discretion within the required timeframe, the reviewing court must apply [a] default de novo standard." *Id*. at 631-32. While, in accordance with the law of trusts, administrators are understood to have expert knowledge of the intricacies of individual cases, "deference to the administrator's expertise is inapplicable where the administrator has failed to apply his expertise." *Id*. at 632. The court does allow "'deemed denied' decisions can be afforded judicial deference if the reviewing court determines that the administrator's initial denial and statement of reasons can effectively be applied to the claimants' appeal." *Id*. at 633. Again, as in *Seman*, the claimant offered significant additional evidence in support of the claim. Rather than "a meaningful dialogue between ERISA plan administrators and their beneficiaries," which might still have resulted in a deferential standard of review, "after more than six months of radio silence...[the administrator] never got around to exercising its discretion or applying its administrative expertise to reach a final decision." *Id.* at 635-36. Because the administrator failed to apply his expertise to the case and instead ceased communication with the claimant despite the claimant's response to the request for additional information, the court remanded the case to the district court with direction to apply a de novo standard of review.

Finally, in ***Jebian v. Hewlett-Packard Company Employee Benefits Organization Income Protection Plan,*** 310 F.3d 1173 (9th Cir. 2002), the Ninth Circuit decided, in an opinion referenced by the *Gilbertson* court, "decisions made outside the boundaries of conferred discretion are not exercises of discretion." *Id.* at 1178. The plan agreement and ERISA contain language that directs participants to "deem denied" appeals after 60 days or, if the plan notifies them in writing of a delay, 120 days. Voluntary Plan Administrator (VPA), HP's independent claims administrator, after denying Jebian's original claim, replied to his appeal 119 days after it was filed. The reply was not a decision, only a notice that his appeal had been received and a decision was pending. The court, with the acknowledgement of leniency after a sixty-day contractual and statutory limitation cut off, deemed the claim denied the following day. The court would "not defer when a decision is, under the Plan, necessarily the mechanical result of a time expiration rather than an exercise of discretion." *Id*. at 1179. As a result, as the plan administrator did not exercise the allowed discretion, the claim was remanded for de novo review and additional evidence could be admitted.

E. Conflicts between SPD and Plan Document.

In ***Burstein v. Retirement Account Plan for Employees of Allegheny Health Education and Research Foundation***, No. 02-2666, 2003 U.S. App. LEXIS 13471 (3rd Cir. July 2, 2003), the Third Circuit ruled, in agreement with nine other circuits, that, "where a summary plan description (SPD) conflicts with the plan language, it is the summary plan description that will control." 2003 U.S. App. LEXIS 13471, at *33. Further, the Court sided with the Sixth Circuit in deciding that reliance on the SPD is not necessary to claim benefits. The, First, Fourth Seventh, and Eleventh Circuits have all held that proof of reliance is necessary.

Allegheny Health (AHERF), a nonprofit, filed for bankruptcy and liquidated its assets. Included in these assets were several hospitals. Several employees of these hospitals filed suit when they were terminated and did not receive their unvested retirement benefits. They alleged that language in the SPD stated their benefits would fully vest upon termination of the plan, as it did partially after the asset liquidation. This language was in conflict with language in the plan document. However, the court quoted the position of the Eleventh Circuit: "'It is of no effect to publish and distribute a plan summary booklet designed to simplify and explain a voluminous and complicated document, and then proclaim that any inconsistencies will be governed by the plan.'" *McKnight v. Southern Life and Health Ins. Co.,* 758 F.2d 1566, 1570 (11th Cir. 1985). Hence, "employees are entitled to rely on the descriptions contained in the summary." *Burstein*, 2003 U.S. App. LEXIS 13471, at *31. Finally, "in addition to the Eleventh and Second Circuits, the Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, and Tenth Circuits have all adopted ... views that if SPD language differs from or conflicts with the plan language, it is the SPD language that will control." *Id.* at *32.

In addition, the Third Circuit determined that "in enforcing an SPD's terms, a participant does not need to plead reliance or prejudice, since the claim for plan benefits under ERISA § 502(a)(1)(B) is contractual." *Id.* at *42

In ***Burke v. Kodak Retirement Income Plan and Kodak Retirement Income Plan Committee***, 2003 U.S. App. LEXIS 14523 (2nd Cir. July 17, 2003), the Second Circuit ruled that, not only does the SPD control over the plan

document when there is conflict, but the circuit also follows a "presumption of prejudice" standard when determining if the participant or beneficiary has a claim against the plan.

Burke was a widowed spouse who, until six months prior to her husband's death, had been a domestic partner for 8 years. She filed for Survivor Income Benefits (SIB), had them denied, and filed an appeal six months later. Although the SPD and denial notification letter stated that she "should" file an appeal within 90 days, the court determined that the language was "grossly uninformative." 2003 U.S. App. LEXIS 14523, at *9. "In fact, in at least sixteen places other than the SIB section, Kodak knew how to employ mandatory language." *Id.* at *10. When Kodak did not employ this language in the SIB section of the SPD, it did not provide sufficient notice of a 90-day limit.

Further, the SPD omitted mention of a required affidavit for a domestic partner to claim SIB. The omission, when compared to the sixteen mentions of affidavit pertaining to other sections in the SPD, led the court to determine that the SPD did not require an affidavit for a domestic partner to claim SIB if evidence of prejudice existed. Finally, accordin gto the court: "The consequences of an inaccurate SPD must be placed on the employer...The result is a presumption of prejudice in favor of the plan participant after an initial showing that he was likely to have been harmed." *Id.* at *23-24.

F. Remedies After *Great-West v. Knudson.*

1. *Administrative Committee of the Wal-Mart Stores, Inc. Associates' Health and Welfare Plan v. Varco,* Nos. 02-3829, 02-1124 & 02-1143, Slip Opinion, (7th Cir. July 29, 2003).

Defendant Varco was injured in an automobile accident and recovered medical expenses from the Wal-Mart health care plan. Varco sued the other driver in the accident and received relief. The Wal-Mart plan initiated this action to recover the medical expenses it had pursuant to the plan. The Seventh Circuit looked to the Supreme Court's *Great-West Life v. Knudson* decision to determine whether the relief requested by the Wal-Mart plan cconstituted equitable relief under ERISA section 502(a)(3)(B) and also ruled on whether the Illinois common fund doctrine for recovery net attorney's fees was preempted by ERISA.

"The committee, as a fiduciary, was seeking to impose a constructive trust on the funds held in Varco's reserve bank account. Unlike the legal action addressed in *Great-West Life,* the funds at issue here are identifiable, have not been dissipated, and are still in the control of a Plan participant due to the fact that [Varco's attorney] placed them in a reserve account in Varco's name when they were disbursed." *Id* at 9. In contrast, in *Great-West*, the funds were placed in a trust in the name of the beneficiary. "Thus, under *Great-West Life,* the reimbursement action by the Committee in this unique case is equitable because the funds the Committee seeks to recover are identifiable, are in the control of a defendant, and the Committee is rightfully entitled to the monies under the terms of the Plan." *Id.* at 10.

In analyzing whether ERISA preempts the Illinois common fund doctrine, the Seventh Circuit stated: "In this case...state law contradicts the terms of the Plan and therefore contravenes ERISA's requirements that plans be administered,

and benefits be paid, in accordance with plan documents." *Id.* at 14. However, "if [Varco's attorney] had not compensated himself fully...then the district court could have properly categorized the action as one by an attorney to enforce his rights and therefore appropriately brought by Varco under Illinois state law." *Id.* at 16. Here, however, because the Illinois statute involved a relationship between a beneficiary and a fiduciary, "the Plan in this case controls the relationship" and the plan terms precluded application of the Illinois common fund doctrine. *Id* at 18.

2. *Rego v. Westvaco Corp*., 319 F.3d 140 (4th Cir. 2003).

The Fourth Circuit interpreted the Supreme Court's decision in *Mertens v. Hewitt Assocs.* in a claim for the difference in value of a depreciated stock fund. According to Fourth Circuit, *Mertens* means that, "the relevant question is not whether a given type of case would have been brought in a court of equity, but whether a given type of relief was available in equity courts as a general rule." *Id.* at 145. Historically, when the bench was divided, courts of equity would only restore property to plaintiffs if it was, in good faith, theirs but was in the defendant's possession.

Rego, after his termination from Westvaco, filed to cash out his stock fund two weeks after the earliest possible cash out date. In those two weeks, the fund depreciated in value. Rego filed a claim to recover the difference in value, which was denied. His claim alleged a breach of fiduciary duty, asserting that the defendants misled him into cashing out his account at the later date. The Fourth Circuit ruled that the relief he sought did not exist under ERISA. While he had suffered loss, there was no benefit to Westvaco, nor did Westvaco control any assets that belonged to Rego. "In this case, defendants possess no particular fund or property that can be clearly identified as belonging in good conscience to the plaintiff." *Id.* at 145.

3. *Honolulu Joint Apprenticeship v. Foster,* 332 F.3d 1234 (9th Cir. 2003).

The Honolulu Joint Apprenticeship and Training Committee (HJA) offered training scholarships to apprentices with their consent to accept union firm employment upon completion of the apprenticeship program. Non-union firm employment required the former apprentice to repay the cost of the training. 2003 U.S. App. LEXIS 12293, at *2.

James Foster completed his apprenticeship and joined a non-union firm but refused to repay the scholarship money. HJA filed suit under ERISA as a fiduciary of the apprenticeship program, an undisputed "welfare benefit plan" under ERISA section 3(1)(A). The Ninth Circuit ruled that HJA could not recover under ERISA § 502(a)(3) because the claim was not equitable. The court declared that the rationale of *Great-West Life v. Knudson,* 534 U.S. 204 (2002), means that "equitable restitution is available where the specific res or funds can be identified and attached by equitable lien or constructive trust, but not where the plaintiff seeks to impose general personal liability as a remedy for the defendant's monetary obligations...There is no indication that the funds are specific or identifiable, or that HJA seeks anything other than monetary compensation on a breach of contract claim." *Id.* at *5 & *8. Therefore, the Ninth Circuit affirmed summary judgment in favor of Foster.

4. *Gerosa v. Savasta & Company, Inc.,* 329 F.3d 317(2nd Cir. 2003).

Savasta & Co. is an actuarial firm representing the Cement Masons Local 780 pension plan. Plaintiffs brought suit for breach of fiduciary duty under ERISA and state law claims including professional malpractice. The Second Circuit ruled that plaintiffs could not recover under ERISA because non-fiduciary defendants could only be held liable for "cash money" damages "under the antique equitable remedy of restitution" when "the defendant holds funds or property that in good conscience should belong to the plaintiff." 329 F.3d at 321. The alleged breach of fiduciary duty did not benefit the defendants, it only derogated the funds of the plaintiffs. The court also ruled that the state law claims were actionable and not preempted by ERISA finding that "ERISA does not preempt 'run-of-the-mill' state-law professional negligence claims against non-fiduciaries." *Id. at 323.*

The Second Circuit analogized the trustees' claim to the fraud claim in *Biondi* (see *supra* for summary of Biondi). Actuaries perform a service that is not necessarily associated with a benefit plan and state law traditionally governs their behavior. *Id.* at 325-26.

G. Plan Participation for Nonemployees as "Beneficiaries"

1. *Ruttenberg v. United States Life Insur.,* 2003 U.S. Dist. LEXIS 7397 (N.D. Ill. May 1, 2003).

Ruttenberg filed state law claims against United States Life for a denial of his disability benefits. The district court ruled that these claims were preempted by ERISA because (1) the plan qualified as an "employee welfare benefit plan" under ERISA and (2) Ruttenberg qualified as a beneficiary. Ruttenberg was designated as class 3 by the plan. His employer paid no premiums on his benefit plan. However, the employer paid premiums for employees in classes 1, 2, and 4. Because the plan qualified as an "employee welfare benefit plan" for some employees, the court treated the entire plan as governed by ERISA. The court said: "While true that the particular class of employees to which Ruttenberg belongs received no funding, this does not negate the fact that contributions are made by the employer to the Plan itself." 2003 U.S. Dist. LEXIS 7397, at *9.

More troubling, the court alternatively decided that Ruttenberg was covered by the plan as a beneficiary. According to the court: "Even if he is not an employee of SMW, he is attempting to receive benefits under the ERISA Plan through which SMW is the participating employer. Ruttenberg, therefore, could only recover under the Plan if he was 'entitled to a benefit thereunder.'" *Id.* at *14. The state law claims were thus preempted by ERISA.

2. *Turnoy v. Liberty Life Assurance Co.,* 2003 U.S. Dist. LEXIS 1311 (N.D. Ill. Jan. 30, 2003).

Turnoy filed state law claims, which were preempted by ERISA, against Liberty Life for denial of his claims under his benefit plan with Mass Mutual. The district court used a three-tiered analysis: The Plan was an "employer welfare benefit plan" under ERISA. Turnoy was a beneficiary under the plan. The state law related to, and did not fall within the savings clause of, ERISA.

The most interesting portion of the opinion is the court's ruling that Turnoy was a plan beneficiary. Turnoy was never an employee of Mass Mutual. Rather, he was classified as an independent contractor. As such, he was not considered a plan participant, but the court ruled he was a beneficiary as defined by ERISA. "Rejecting the plaintiff's argument that the definitions of 'beneficiary' should be limited to persons such as spouses and dependents," the district court was "persuaded by 'the unremarkable conclusion that ERISA's definition of beneficiary means precisely what it says." 2003 U.S. Dist. LEXIS 1311, at *15 & *14. Because the plan was an ERISA welfare benefit plan, Turnoy was a plan beneficiary, and his claims related to the plan, the district court dismissed the his state law claims with leave to refile under ERISA.

H. ESOP

1. Chao v. Hall Holding Co., 285 F.3d 415 (6th Cir. 2002).

The Secretary of Labor brought suit against the fiduciaries of an ERISA Employee Stock Ownership Plan (ESOP) alleging breach of fiduciary duty and a prohibited transaction associated with the purchase of 9.96 percent of Hall Holding Co., Inc. The court ruled on three matters: Whether there was adequate showing of material fact that the defendants had breached their fiduciary duty? Whether the actions of a reasonable hypothetical fiduciary are relevant to a section 406(a)(1) violation? And whether the District Court erred in its assignment of damages? 285 F.3d at 419-20.

The Court determined that, although the defendants relied on an analyst expert in determining the value of the stock, this reliance was not a defense because they had failed two parts of the three-part reliance test. While they had examined the expert's qualifications, (1) they had not provided the expert with complete and accurate information – specifically, they had asked the analyst to value a company rather than a minority stake in the company, which stake they intended to purchase – and (2) their reliance on the information was not justified because they used the valuation to set a price for a different company – Hall Holding Co., not Hall Chemical.

The court also identified other fiduciary failures: "Essentially, the facts demonstrate that the Hall Chemical ESOP was established in an environment where the trustees were unaware of what was going on, the trustees were not consulted on major decisions affecting the Hall Chemical ESOP, there was no negotiation as to the price of the Hall Holding stock, there was more concern for the return on investment for the Master Trust [an unaffiliated lender], and the inconvenience of dealing with uneven numbers could justify charging the Hall Chemical ESOP an additional $44,900.00 for the stock it purchased." *Id.* at 434-35. As a result, the defendants were found to be in violation of their fiduciary obligation."

The Court ruled that a hypothetical fiduciary test was unnecessary in analysis of prohibited transaction claims. According to the court: "Basically, in creating § 406(a), Congress intended to create a category of per se violations." *Id.* at 439. The actions of other, hypothetical, fiduciaries is not a defense because "it is not enough that a fiduciary, by chance, arrived at fair market value...a pure heart and an empty head are not enough." *Id.* at 437.

Finally, in answering the defendants' claim that the district court's remedies, "would constitute...benefits for the ESOP participants that they never earned nor expected, nor...could obtain legally under the Internal Revenue Code," the Court stated that "benefits...are not a gratuity...but a form of deferred wages and "a district court is given wide latitude in compensating the participants in an ESOP when a breach of fiduciary duty has been shown." *Id.* at 444 (internal citations omitted).

2. *Benefits Comittee of Saint-Gobain Corp. v. Key Trust Co.,* 313 F.3d 919 (6th Cir. 2002).

Furon Company created a leveraged ESOP by loaning approximately $6 million of company stock to the ESOP. However, Furon did not secure the loan. Saint-Gobain Corp. acquired Furon for cash, including the stock held by the ESOP. After the acquisition, Saint-Gobain terminated the ESOP. The trustee of the Furon ESOP distributed the excess funds to the individual accounts less the balance of the loan. Finally, the trustee and the benefit committee filed suits against each other raising the question: "Whether authorizing repayment by the Furon ESOP of its loan from the Company would cause the Trustee to violate its fiduciary obligations under ERISA to the participants of the Furon ESOP." *Id.* at 931-32. Since the loan was unsecured, there would be no recourse for Saint-Gobain and therefore the participants could benefit from a refusal to repay.

The court looked to the intent of Congress in ERISA. "The only interest that the participants have in that money is a residual interest in the event that it cannot be paid, a sort of remainder interest...The remainder only arises as a result of ERISA's prohibiting repayment of the loan, and ERISA's asserted prohibition depends exclusively on the existence of the remainder...The intent of the statute and these safeguards is not furthered by such a technical reading." *Id.* at 932. Therefore, the court ruled that repayment of the loan would not be a breach of the Trustee's fiduciary duty.

IV. AGENCY ACTIONS

A. DOL

1. Expense Allocation in DC Plans. Field Assistance Bulletin 2003-03.

The DOL distributed Field Assistance Bulletin 2003-3 (FAB) to clarify in part and also reverse in part its previous stance on DC plan cost allocation among participants and beneficiaries. While granting exceptional latitude to plan fiduciaries, the FAB also admonishes fiduciaries to be "prudent" and not "arbitrary." The FAB reversed the DOL's previous stance that if costs were not expressly allowed by ERISA to be charged on an individual basis, then they could not be charged on individual basis. The FAB lists five specific costs that are allowed to be charged on an individual basis with the implication that they are not exclusive. Along with these examples, the tenor of the FAB encourages fiduciaries to carefully choose the most appropriate method of group cost allocation. While pro rata and per capita allocation methods are contrasted, the FAB also opens the door for other utilization methods of cost allocation. In general, as long as the method of allocation is not expressly forbidden by ERISA

and "provided a rational basis exists for the selected method," "plan sponsors and fiduciaries have considerable discretion in determining...how plan expenses will be allocated."

2. Plan Loans to Officers and Directors. Field Assistance Bulletin 2003-01.

The DOL opined that the denial of loans, to officers and directors in a publicly held company, based on a possible conflict with the new addition by the Sarbanes-Oxley Act to the 1934 Securities Exchange Act, did not constitute a violation of ERISA's requirement that loans be available to all participants and beneficiaries on a reasonably equivalent basis.

3. Health Care Continuation Proposed Regulation. May 28, 2003.

The Department of Labor issued proposed new regulations for COBRA notification. "The proposed rules set minimum standards for the timing and content of the notices required under the continuation coverage provisions and establish standards for administering the notice process." (Proposed Regulation p. 1) While the regulations are currently in porposed status, the DOL has indicated that in some instances they simply restate current law. Further, the proposals may become effective for new plan years beginning January 1st, 2001. The new guidelines focus on four areas: (1) the general continuation of coverage notice, (2) notice requirements for employers, (3) notice requirements for employees, and (4) notice requirements for administrators. Included in the proposed guidelines are proposed model notices. The old model general notice is no longer is considered to be in good faith compliance. Observance of the new regulations may require a rewriting of current notices and procedures. In addition, a notice giving reason for any denial of continuation, not currently required, will be required.

4. Sarbanes-Oxley black-out periods.

DOL and SEC issued final regulations in January 2003 implementing the black-out periods mandated by Sarbanes-Oxley. Essentially, the rules require advance written notice to participants before the plan temporarily suspends participants' rights to direct their defined contribution plan investments. Also, the regulations require plans to prohibit insiders from trading in employer stock during black-out periods. The penalties for non-compliance are substantial, including a civil penalty of up to $100 per day per participant. Furthermore, late provision of the required written notice does not terminate the penalty, but it may be a factor to be taken into account when assessing the penalty. For violation of the insider trading ban, the insiders face both SEC sanction and private suits for recovery of the profits realized in the trading.

B. IRS

1. Cash Balance Plan Proposed Regulation re: application of age-discrimination rules.

The proposed regulation provides that 'typical' cash balance plans do not violate the prohibition in § 411(b)(1)(H) on reductions in benefit accrulas because

of the attainment of any age. IRS held public hearings on the proposed regulation on April 9 and 10 at which a wide variety of opinions were offered. In its words, in its Summer 2003 edition of Employee Plans News, "The next step is for Treasury and IRS to consider all comments submitted – including those at the public hearing – and to move forward." P. 10 In the meantime, the moratorium on determination letters continues to be in effect.

2. Expense Allocation in DC Plans.

The IRS has questioned whether fees might violate the Treas. Reg. sec. 1.411(a)-11(c)(2) prohibition on a "significant detriment" on separating participants who maintain their plan accounts. According to the Summer 2003 edition of Employee Plans News, "The IRS hopes to clairy soon the tax plan qualification issues raised in the FAB related to Code sections 401(a)(4) and 411."

3. Catch-up Contribution Regulations.

EGTRRA permited participants age 50 or over to make contributions to a variety of qualified defined contribution plans that exceed the 'normal' maximum limitation. In July, 2003 the IRS published final regulations on those contributions, which have come to be known as "catch-up" contributions. In general, the final regulations track the proposed regulations and provide guidance on both calculation of the catch-up contribution amounts and eligibility to make those contributions. Those regulations apply to contributions in taxable years beginning on or after January 1, 2004.

3. Revised 401(k) Regulations.

The IRS issued lengthy new proposed regulations on 401(k) plans. Because of the popularity of 401(k) plans and the technical nature of theproposed regulations, those regulations deserve more attention than can be given in this format. However, some of the highlights include:

-- continued support for the use of automatic enrollment programs,
-- restrictions on the use of qualified nonelective contributions used to enable a plan to pass the actual deferral percentage (ADP) test
-- more guidance on hardship distributions

4. Second White Paper on "The Future of the Employee Plans Determination Letter Program, May 1, 2003.

In 2001 the IRS issued a white paper inviting discussion on modifications to the determination letter process. In its 2003 White Paper, the Service indicated that, of the many options outlined in the first paper, three possible approaches remained viable. One, third-party certification, has been put in abbeyance for the time being. That leaves two possibilities. The first is to maintain the status quo. The second is to establish as system with staggered remedial amendment periods. In short, staggered amendment periods would help even work flow for plan sponsors, lawyers, and the IRS. But, commentators raised concerns with complexities such as plan mergers. The IRS outlined a method for dealing with those complexities. The IRS also noted one additional alternative suggested by a commentator – annual amendments and determination letters. The IRS iinvited additional public comment that is due on September 2, 2003.

5. Retroactive Annuity Starting Dates and Delayed QJSA Explanations.

Final regulations effective July 16, 2003 for plan years beginning on or after January 1, 2004 explain the approach to be taken if a plan wishes to provide the required QJSA explanation after the annuity starting date. The regulation also provides guidance on the effect of adjustments that must be made because of the retroactive nature of the annuity election.

6. Deemed IRAs.

The IRS released proposed regulations on May 20, 2003 supporting the concept of deemed IRAs and giving guidan ce to plan sponosrs who wish to incorporate traditional or Roth IRAs within a qualified plan. As a general matter, the proposed regulations provide that the IRA and not the qualified plan rules apply to the deemed IRAs but the rest of the plan remains subject to the qualified plan rules. Comments are due by mid-August.

7. Plan Loans.

In December 2002, the IRS issued final regulations on plan loans that are effective for plan loans made on or after January 1, 2004. The final rules generally followed the substance of the proposed rules. The regulations address topics including extension of repayment periods in cases of military service, loans that are refinancedmultiple loans and the ability of a plan to rely on employee certification of prior loan status.

C. Other

1. Retiree Medical coordination with Medicare.

In July 2003 the Equal Employment Opportunity Commission issued a proposed exemption from the Age Discrimination in Employment Act for medical plans that make different medical benefit provisions for retirees who are Medicare-eligible as compared to those who are not eligible for Medicare. The proposed exemption makes clear that the exemption extends only to medical benefits provided for retirees and does not affect ADEA protections for active employees or for other types of benefits.

Employee Benefits: Year in Review

Dana Muir, Louis and Myrtle Moskowitz
Research Professor of Business and Law and
Associate Professor of Business Law
University of Michigan Business School
dmuir@umich.edu
http://www.bus.umich.edu/FacultyBios/FacultyBio.asp?id=000279015

Overview

- Court Decisions
  - Supreme Court, Cash Balance, Enron, Misc.
- Agency Actions
  - DOL and IRS
- Legislative Outlook
  - DB Plan Funding
  - Other Possibilities

Supreme Court – 2003

- Kentucky Assn. of Health Plans v. Miller, 123 S. Ct. 1471
  - New preemption test for insurance savings clause.
    - State law must be specifically directed toward entities engaged in insurance AND state law must substantially affect the risk pooling arrangement between the insurers and the insured.
  - Portends: Broader scope for savings clause. Perhaps willingness of Court to re-look at preemption.

Supreme Court – 2003

- **The Black & Decker Disability Plan v. Nord, 123 S. Ct. 1965**
  - Treating physician rule (from Social Security) is not the appropriate standard for ERISA benefit denial cases.
  - But, says that "Plan administrators, of course, may not arbitrarily refuse to credit a claimant's reliable evidence, including the opinions of a treating physician."
  - Portends: Continued deference to plan administrators in eligibility determinations. But, standards for when a conflict of interest exists and the analysis used to evaluate the administrator's decision will remain inconsistent across circuits.

Supreme Court – 2004/5

- Yates v. Hendon, 287 F.3d 521 (6th Cir. 2002) cert granted
  - Is a worker-owner an ERISA participant?
  - Circuit split: First and Sixth hold that sole shareholders are not participants whereas the Fourth and Fifth disagree.
  - Important in small entities. May provide some signals about definition of a participant for whether non-employees may be beneficiaries of ERISA plans.

Supreme Court – 2004/5

- **Cline v. General Dynamics, 296 F.3d 466 (6th Cir. 2002) cert granted**
  - Does ADEA prohibit reverse discrimination?
  - Context was a collective bargaining agreement that grandfathered workers age 50 with 30 years of seniority into eligibility for retiree health coverage.
  - EEOC supports Sixth Circuit decision that ADEA prohibits reverse discrimination. Circuits are split on this issue.
  - Sixth Circuit's approach calls into question a variety of benefit practices that differentiate employees based on an age over 40 (for example diversification rights in an ESOP).

Cash Balance Plans

- **Cooper v. IBM Pension Plan, 2003 U.S. Dist LEXIS 13223**
  - Cash balance plan violates ERISA's prohibition on reduction of benefit accruals on account of age.
  - Contrary: Proposed Treasury/IRS regulations and Eaton v. Onan, 117 F. Supp. 2d 812 (S.D. Ind. 2000).

Cash Balance Plans

- Berger v. Xerox Corp. Retmt. Inc. Guar. Plan., 338 F.3d 755
  - Crediting interest for lump sum calculations at the PBGC rate rather than at the rate specified by the plan for 'normal' interest crediting violates the requirement that accrued benefits be the actuarial equivalent of a benefit commencing at normal retirement age.

Tittle v. Enron Corp., 2003 WL 22245394

- Claims proceed against:
  - Northern Trust Co.
  - Enron, Officers, Compensation Committee and Plan Administrative Committee
  - Arthur Anderson – state law negligence claims only

Tittle v. Enron Corp., 2003 WL 22245394

- **Northern Trust Co.**
  - **A "directed trustee retains a degree of discretion, authority and responsibility that may expose him to liability…"**
    - Focused on alleged red flags regarding financial health of plan sponsor and "regular reviews of the company's financial statements."
  - **A directed trustee must determine whether directions from named fiduciary "are 'proper' and facially in compliance with the terms of the plan and ERISA."**

Tittle v. Enron Corp., 2003 WL 22245394

- **Officers and Directors**
  - They have potential personal liability even if they do not have an individual discretionary role in plan administration.
  - The court will "make a functional, fact-specific inquiry to assess 'the extent of responsibility and control exercised by the individual with respect to the Plan.'"
  - Those who appoint plan fiduciaries have the "duty to insure that the selected fiduciaries in turn complied with their fiduciary duties."

Tittle v. Enron Corp., 2003 WL 22245394

- 404(c) Protections
  - Burden of establishing compliance with 404(c) is on defendants. Here have issues with transferability of assets and adequacy of information.
  - Even if 404(c) protections apply, the court accepted the DOL's argument that selection and monitoring of investment choices is a fiduciary function.
  - The plan terms required fiduciaries to ensure diversification of plan investments.

Tittle v. Enron Corp., 2003 WL 22245394

- Disclosure
  - Rejected argument that increased disclosure to plan Ps and Bs would necessarily have caused defendants to violate federal securities laws.
  - Courts continue to struggle with the scope of disclosure requirements. The court states the Fifth Circuit's position as: "in addition to a specific inquiry from a plan participant, special circumstances with a potentially 'extreme impact' on a plan as a whole, where plan participants generally could be materially and negatively affected, might support imposition of such an affirmative duty [of disclosure] in a particular case."

Other Case Law

- **Preemption:** Continuing to permit more state law to survive (fraud).
- **Remedies:** Issues about the scope of equitable relief continue after *Great-West*. Fiduciary cases are not being distinguished. Back pay to be addressed by Tenth Circuit in *Milsap v. McDonnell Douglas.*
- **SPD and Plan Document Conflicts:** More participant protective.
- **Limiting § 409 DC Actions:** Argument that relief must flow to the plan *as a whole* is being rejected.

DOL Actions

- **Expense Allocation in DC Plans.**
  - Modified and clarified past position to permit broader allocation of costs to Ps & Bs.
  - Query whether allocations might be a 'significant detriment' to separating participants and thus violate IRC qualification requirements. IRS to clarify.
- **Plan Loans to Officers & Directors** – Plans may preclude without violating ERISA's 'equal availability' requirement.
- **COBRA Notifications** – Extensive changes, including new requirement for notice of denial.
- **Sarbanes-Oxley Black-out Periods** – Detailed guidance with substantial penalties for noncompliance.

Treasury/IRS Actions

- **Cash Balance Plan Proposed Regs** – Provide that a variety of typical CB formulae do not violate the IRC's prohibitions on age discrimination. Controversial hearings. Withdrew comparability proposal.
- **Catch-up Contribution Final Regs** – Generally track proposed regs and cover both amount and eligibility for contributions.
- **401(k) Proposed Regs** – Comprehensive including testing.
- **White Paper on Future of Plan Determination Letters** – Appears likely either status quo or staggered remedial amendment periods.
- **Deemed IRA Proposed Regs** – Regulation tracks IRA rules not qualified plan rules.

Legislative Proposals

- **Discount Rate for DB Plan Liabilities**
  - Short term fix likely
  - Longer term – review of funding rules
- **Others Under Discussion**
  - Investment advice
  - Right to diversify 401(k) assets
  - Increased information on benefits statements
  - Accelerate vesting in DC plans
  - Executive nonqualified plans

EMPLOYMENT LAW YEAR IN REVIEW

October 10, 2003
ACC Annual Meeting

Patti E. Russell
Associate General Counsel and Senior Employment Counsel
Becton Dickinson and Company

FLSA - REMOVAL

Breuer v. Jim's Concrete of Brevard, 123 S.Ct. 1882 (2003)

Supreme Court held that defendant may remove FLSA cases to federal court.

- Plaintiff Breuer filed State Court action alleging violation of FLSA. Defendant removed to federal court under §1441(a).
- Breuer claimed Plaintiff had right to choose forum under FLSA.

Breuer

Plaintiff tried to remand based on

- FLSA provision "an action to recover … may be maintained … in any federal or state court of competent jurisdiction."

  - 11th Circuit held that FLSA did not satisfy requirement of §1441(a) that any prohibition of removal be "expressly provided by Act of Congress." Supreme Court affirmed.

Practice Pointer:

- Employers may remove FLSA cases if federal court is superior forum strategically.

TITLE VII

Desert Palace Inc. v. Costa, 123 S.Ct. 2148 (2003)

Supreme Court held that:

Direct evidence of discrimination not required for "mixed motive" jury instruction under Title VII.

- Plaintiff Costa, warehouse and heavy equipment worker, only woman employee.
- Costa had problems with co-workers that led to discipline and termination.
- Costa alleged sex discrimination/sexual harassment.

Desert Palace

District Court

- Mixed motive instruction to jury: **Even if employer also motivated by lawful reasons, plaintiff entitled to damages if sex was motivating factor.**

Ninth Circuit

- Evidence sufficient for jury instruction, and reasonable jury could have found sex was motivating factor.

Desert Palace

Supreme Court

- Upheld – direct evidence not required. Plaintiff must only demonstrate employer used forbidden consideration.

Pointers:

- Plaintiffs can obtain mixed motive instruction with modest discrimination evidence.
- Shifts burden to employers to demonstrate same result, even if no discrimination.

AFFIRMATIVE ACTION

Grutter v. Bollinger, 123 S.Ct. 2325 (2003)

Supreme Court upheld Law School policy that uses race in admissions decisions.

- No violation of Equal Protection Clause, Title VII, or 42 U.S.C. §1981.
- Diversity is compelling interest, justifying narrowly-tailored use of race in selecting applicants.

Grutter

- White female, applied to University of Michigan Law School – denied.
- Grutter argued:
  1. School used race as predominant factor, giving minorities greater chance.
  2. No compelling interest.
- No quotas, but used race as one of many factors.

Grutter

Supreme Court held use of race to further compelling interest of diverse student body not prohibited.

- School did not have to exhaust all race-neutral means before using race.
- Admissions policy OK because allows for individualized review.
- Race-conscious admissions policy should be limited in duration.

Grutter

Pointers:

- Implications beyond educational institutions.
- Admissions can be analogized to hiring decisions to justify race as a factor among others in employment context.

Gratz v. Bollinger, 123 S.Ct. 2411 (2003)

In contrast, Supreme Court held University of Michigan's race-based policy for undergraduate admissions violated the Equal Protection Clause, Title VII, and 42 U.S.C. §1981.

- Admissions policy assigned points to such categories as grade point average, test scores and leadership activities.
- Automatically awarded one-fifth of points necessary for admission to students from underrepresented minority groups.

Gratz

- As in Grutter, Supreme Court held that University had compelling interest – BUT policy NOT narrowly tailored to serve compelling interest.
- Policy failed under strict scrutiny.

FMLA

Nevada Department of Human Resources v. Hibbs, 123 S.Ct. 1972 (2003)

Supreme Court upheld right of public employees to sue state under FMLA.

- Hibbs took time off to care for sick wife. Applied for FMLA leave, but told leave taken under Nevada state policy counted against his FMLA leave.
- Employer insisted Hibbs return to work because exhausted FMLA leave. He refused and was fired.

Hibbs

Hibbs sued:

- Protections of FMLA should be extended to state employees to remedy past gender discrimination in leave benefits.

Supreme Court acknowledged 11th Amendment state protection against federal lawsuits, but recognized immunity is subject to limitations.

Hibbs

- Congress can abrogate state immunity if:
  - ✓ use clear language in statute
  - ✓ remedied an existing injury
- FMLA enacted to remedy gender discrimination and widespread pattern of treating men and women differently as to family leave benefits.
  - Court distinguished decisions involving ADA and ADEA.

Pointer:
State employees can sue for damages if denied FMLA rights.

ARBITRATION

Green Tree Financial Corp. v. Bazzles, 123 S.Ct. 2402 (2003)

Supreme Court held decision as to whether arbitration agreement permits class certification is for arbitrator

- Bazzles entered into lending contract with clause providing for arbitration of all contract-related disputes.
- Bazzles filed suit, claiming contract form should have advised of right to select own attorneys and insurance agents.
- Bazzles moved for class certification, and Green Tree moved to compel arbitration.

Green Tree

- State Court certified class and compelled arbitration on class basis.
  - Arbitrator awarded damages and attorneys' fees
- Green Tree claimed class arbitration not permissible.
- South Carolina Supreme Court allowed class action because arbitration clause silent.

Green Tree

Supreme Court held contracts not clear on arbitration on class-action basis.

- Arbitration agreement granted broad authority to arbitrator.
- Arbitrator should decide whether case should proceed as class-action.
- Arbitration is matter of contract, and any doubt should be resolved in favor of arbitration.

Pointer:
Make clear in arbitration agreements that class actions not permissible.

ARBITRATION

EEOC v. Luce, Forward, Hamilton & Scripps, 2003 U.S. App. Lexis 20007, No. 00-57222 (9th Cir. 2003)

Ninth Circuit held Title VII does not bar compulsory arbitration agreements.

- Applicant at law firm denied employment because he refused to sign arbitration agreement.
- Successfully sued employer in state court, then EEOC brought action on applicant's behalf in federal court alleging retaliation and seeking damages.

EEOC v. Luce

- EEOC also sought permanent injunction forbidding employer to require employees to sign arbitration agreements.

  - District Court enjoined employer from requiring applicants to agree to arbitrate Title VII claims or enforcing existing agreements.

- On appeal, Ninth Circuit held nothing in Title VII prevents use of arbitration to resolve claims.

Pointer: Helpful precedent for requiring employees to agree to mandatory arbitration.

ADA - Definition of "Employee"

Clackamas Gastroenterology Assocs., P.C. v. Wells, 123 S.Ct. 1673 (2003)

Supreme Court adopted EEOC approach, focusing on the common law element of control and the six-factor test.

- Bookkeeper sued medical clinic for disability discrimination under the ADA.
- Clinic argued not covered by ADA because did not employ at least 15 employees.
  - Physicians were shareholders and directors, not employees.

Clackamas

Supreme Court noted ADA, like many other federal laws, does not define "employee."

- Congress definition: "individual employed by employer" is circular and useless.

Common law element of "control" is principal guidepost

- If physicians operate independently and manage the business -- NOT employees.
- If subject to firm's control -- employees.

Clackamas

Six factor test:

1. Whether organization can hire or fire or set work rules.
2. Whether and to what extent organization supervises the individual's work.
3. Whether individual reports to someone higher in the organization.
4. Whether and to what extent individual can influence the organization.
5. Parties intent as to whether individual is employee – look at contracts.
6. Whether individual shares in profits, losses and liabilities.

Clackamas

Supreme Court held whether shareholder-director is employee "depends on all the incidents of the relationship … with no one factor being decisive."

- Case sent back to district court for further proceedings.

Pointers:

- Disgruntled "partners" may be more likely to sue partnerships and professional corporations.
- Such corporations and partnerships should consult with counsel on their manner of operation and internal procedures.