

THE LABOR LAWYER

A Journal of Ideas
and Developments
in Labor and Employment Law

Volume 21, Number 2 • Fall 2005

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EDITORIAL STATEMENT: *The Labor Lawyer* is a journal of ideas and developments in the field of labor and employment law. Its objectives are to provide practitioners, judges, administrators, and the interested public with balanced discussions of developments in all areas of labor and employment law. *The Labor Lawyer* is geared to the practical needs of those who work in this area and seek to share their insights and viewpoints. The Editor encourages discussion of the broader policy issues that underlie these developments. *The Labor Lawyer* may be cited as follows, by volume and page: 20 LAB. LAW. — (2005).

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FREQUENCY AND POSTAGE: *The Labor Lawyer* (ISSN: 8756-2995) is published three times per year by the American Bar Association, Section of Labor and Employment Law. Third-class postage is paid at Chicago, IL, and additional mailing offices.

ADDRESS CHANGES: Send all address changes to *The Labor Lawyer*, ABA Service Center, American Bar Association, 321 North Clark Street, Chicago, IL 60610-4714; phone: 312/988-5522; fax: 312/988-5528; e-mail: abasvcctr@abanet.org.

INTERNET ACCESS: Visit *The Labor Lawyer* home page at Syracuse University: www.law.syr.edu/labor_law; and our ABA Web site at BNA Books: www.bna.com/bnabooks/ababna/laborlawyer.htm.



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A Journal of Ideas
and Developments
in Labor and Employment Law

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The Editor's Page

"Continuity gives us roots; change gives us branches, letting us stretch and grow and reach new heights." Pauline R. Kezer. "But times do change and move continually." Edmund Spenser. *The Labor Lawyer* has seen some changes in the editorial process, and has continued to grow this year with the addition of Professor Kate Dole as the Associate Editor. I have found that as I now begin what will be my last semester in law school, I have barely begun to realize the impact of upcoming changes, and I have begun to embrace the idea of change as growth.

As I reflect over the year, I have witnessed the significant changes in a long standing United States Supreme Court: the appointment of a new Chief Justice, John Roberts following the death of former Chief Justice William Rehnquist. Additionally, the retirement of the first woman to serve on the court, Justice Sandra Day O'Connor, and the appointment of Justice Samuel Alito.

This year I was privileged to be the editor-in-chief of the American Bar Association's *The Labor Lawyer*. This journal has given me the opportunity to be a part of the cutting-edge issues in labor and employment law. I would like to thank my family. I would also like to thank, in particular, my articles editors, Matthew Brigham and David Sobotkin, for their tireless dedication to the journal. Without their hard work, the journal would not be the product we have turned out this year. Additionally, I want to thank all the staff of *The Labor Lawyer*, who spent a great amount of time scouring the library, checking citations. Finally, to the faculty advisors Professor Robert Rabin and Professor Kate Dole, for believing in me, for giving me this opportunity, and for their guidance.

This issue of *The Labor Lawyer* contains the annual review of the Supreme Court's labor and employment docket for 2005 written by Professor Samuel Estreicher, who teaches at New York University School of Law. Estreicher commences the review by discussing the changing United States Supreme Court after the retirement of Justice Sandra Day O'Connor. It observes the difference between Justice O'Connor's judicial conservatism in contrast to Justice Scalia's political conservatism, and questions how the new Justice Roberts will fit into the "O'Connor-Scalia divide." The review then moves on to look at the implications of *Smith v. City of Jackson*. Estreicher also provides a discussion on the *Jackson v. Birmingham Board of Education* case, which answered the question of "whether Title IX of the Education Amendments of 1972's protection against sex discrimination by recipients of federal financial assistance applies to retaliation by indirect-victim third parties for reporting prohibited discrimination." *Spector v. Nor-*

wegian Cruise Line Ltd. is also examined in the review, and the review draws to an end by listing the remaining cases reviewed, as well as those cases that have been granted a review by the court for the next term.

This issue contains a series of articles that hit on a variety of hot-button topics, ranging from rights of transsexuals in the workplace to noncompete agreements for temporary employees. In “The Expanding Rights of Transsexuals in the Workplace,” Neil Dishman discusses the rights of transsexuals. Dishman sets forth in his article the developing issue of transsexuals as a protected class. The article examines how some courts are now allowing transsexuals to maintain claims of sex or disability discrimination under Title VII, while others are explicitly forbidding it. The article looks at the implications of state and federal law on the topic, and ends by discussing transsexual discrimination as “sexual orientation” under state law.

Daniel Westman takes an in-depth look at the whistleblower provisions of the Sarbanes-Oxley Act. He begins by discussing the differences between the current whistleblower provisions under Sarbanes-Oxley and the previous laws under state and federal law. Westman examines how the new whistleblower provisions affect state law, and finishes by discussing the implications of these provisions on corporate governance practices.

Richard McCracken’s article, entitled, “San Manuel Indian Bingo and Casino: Centrally Located in the Broad Perspective of Indian Law,” provides insight into how federal laws will be applied to Indian enterprises such as casinos. The article lays out the general law of Indian sovereignty and moves on to discuss the analysis of applying federal rules to the Indian enterprises. McCracken discusses the Coeur D’Alene analysis, which has allowed labor and employment law to be applicable to Indian enterprises. He concludes the article by showing how the NLRB has followed the federal courts in applying the National Labor Relations Act to businesses located on Indian reservations. A companion article, written by Anna Wermuth, appeared in Volume 21, No. 1 of *The Labor Lawyer*. Both papers had been presented at the 2005 Mid-winter Meeting of the American Bar Association’s Committee on the Development of the Law Under the National Labor Relations Act.

William Doyle describes the implications of *Smith v. City of Jackson* on Equal Pay Act (EPA) claims and sex-based pay discrimination claims under Title VII. In his article, Doyle provides an analysis of this case, including the implication that “disparate impact claims are not cognizable under the EPA and that the EPA’s ‘any other factor other than sex’ affirmative defense can be sustained by a factor that is ‘reasonable or unreasonable.’”

This issue concludes with an article by William Pilchak that examines noncompete agreements for temporary employees. Pilchak’s ar-

ticle analyzes possible reasons for the disparities among courts in whether noncompete agreements should apply to temporary employees.

Overall, this issue provides a number of interesting articles that I hope you will enjoy.

Jennifer L. Maxwell

Review of the Supreme Court's Labor and Employment Docket, O.T. 2005

Samuel Estreicher*

I. Foolhardy Predictions

This cannot be the usual end-of-term reprise of the Supreme Court's work. This year, there is essentially one question, one discussion. Any backward-looking review of this term's decisions, or any forward-looking summary of those on the Court's docket in the labor and employment area, or, indeed any other area, necessarily has to deal with the changing composition of the Court.

The confirmation of D.C. Circuit Judge John Roberts as the new Chief Justice of the United States, replacing the late William H. Rehnquist, and the pending nomination of Third Circuit Judge Samuel Alito to occupy the position opened by the announced retirement of Justice Sandra Day O'Connor will represent a significant shift in the future direction of the high court. Very much the successor to Justice Lewis F. Powell Jr. in both temperament and role as the Court's moderate, pragmatic voice, O'Connor so often has cast the decisive swing vote in so many areas that many a brief has been written exclusively with her views and predisposition in mind.

Roberts, who has only been on the bench since 2003, is something of an unknown quantity. He has been an extraordinarily gifted Supreme Court advocate, one of the very few "must-consider" lawyers for any client with a case before the high court. I always tell my students "I can tell you what will happen in 100 years, but don't ask me what will happen tomorrow." Predictions about the future behavior of Supreme Court justices are especially hazardous duty. A good number of presidents have been disappointed in their judicial appointments. President Theodore Roosevelt is reported to have quipped of Justice Oliver Wendell Holmes, "I could carve more backbone out of a banana." And

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certainly, President Eisenhower bewailed his Republican appointees, Chief Justice Earl Warren and Justice William J. Brennan, who effectively turned into political liberals and judicial activists once on the high bench. Justices Harry Blackmun and David Souter are only the most recent examples.

For this audience, however, I will venture on a limb: By all appearances, Judge Roberts seems a reliable conservative, but more of the Powell-(Potter) Stewart-(John M.) Harlan type than the (Antonin) Scalia-(Clarence) Thomas variety. Perhaps it is safer to say he will be a mix of the two. (Judge Alito has not been confirmed as of this writing; I will reserve any predictions as to his influence.)

In order to provide a sense of Judge Roberts' likely role, I will employ academic's license to provide a crude breakdown of the Court's voting blocs. A healthy majority of the Court's work involves the resolution of intercircuit conflicts where the outcome is rarely in doubt, and the Court often renders a unanimous opinion. But for the controversial cases involving deeply held moral beliefs and values, the Court tends to break down into two reliably predictable wings: the liberal "gang of four" and the conservative "gang of three." The Court's liberal grouping is comprised of Justices John Paul Stevens, Ruth Bader Ginsberg, Stephen Breyer, and David Souter. Its conservative wing consists of Chief Justice William Rehnquist, Justice Antonin Scalia and Justice Clarence Thomas. Justice Anthony Kennedy often votes with the conservatives, except in certain areas like First Amendment and personal autonomy cases where he is likely to cast his lot with the liberal wing.

Justice O'Connor has, of course, been the most unpredictable of the Justices, and as a consequence has been the critical fifth vote in several areas of major controversy. Consider these five examples:

- Church-state
 - *Van Orden v. Perry* (4 + 1 vs.; O'Connor dissents)¹
 - *McCreary Co. v. ACLU* (5-4; O'Connor joins and writes concurrence)²
- Affirmative action
 - *Grutter v. Bollinger* (5-4; O'Connor writes for the majority)³
- Federalism
 - *Tennessee v. Lane* (5-4; O'Connor joins majority)⁴
- Campaign finance
 - *McConnell v. FEC* (O'Connor and Stevens write lead opinions)⁵

1. *Van Orden v. Perry*, 125 S. Ct. 2854 (2005).
 2. *McCreary County v. ACLU*, 125 S. Ct. 2722 (2005).
 3. *Grutter v. Bollinger*, 539 U.S. 306 (2003).
 4. *Tennessee v. Lane*, 541 U.S. 509 (2004).
 5. *McConnell v. FEC*, 540 U.S. 93 (2003).

- Abortion
—*Stenberg v. Carhart* (partial-birth ban) (5-4; O'Connor writes concurrence)⁶

Justice O'Connor came to this role honestly. A conservative by instinct and upbringing, she earned her spurs as a state legislator. She has been more a judicial conservative than a political conservative in her decisions. Judicial conservatives believe in a limited judiciary, care about the facts of a particular case, decide cases narrowly, are reluctant to overturn precedent, and are mindful of the likely practical consequences of a ruling. They also tend to defer to policymaking by Congress and the states. These virtues are not present in every O'Connor opinion, but they are present in a good many of them.

By contrast, Justice Scalia has been more of a judicial activist. He may consider himself a political conservative, but he is quite open to, and actively seeks to prod, change. In constitutional cases in particular, he believes in "originalism," a doctrine that holds that judges should always read constitutional text in light of the original intent of the framers. The doctrine may provide a useful counterweight to a more free-ranging "purposive" stance that allows judges to function as an ongoing constitutional convention that reads the text in light of changing realities. But it also allows Justice Scalia and his like-minded colleagues to be more willing to upset longstanding precedent in the interest of restoring the original meaning of the Constitution.

Where will a Justice Roberts fall along the O'Connor-Scalia divide? It is undoubtedly too early in the game even for this foolhardy academic. Judge Roberts has been telling his senatorial interviewers that he believes in *stare decisis* and will vote to overturn precedent only in the most extreme of cases. This may be an instance of "confirmation conversion," but I suspect he is being forthright about his judicial instincts. This suggests a more cautious conservatism than we have seen from Justices Scalia and Thomas in constitutional cases. More I cannot say.

II. Part 2: Review of the Past Term

Getting down to business, and turning to the Court's labor and employment docket for October Term, 2004, we can see several key labor and employment cases in which Justice O'Connor exercised a pivotal influence.

A. *Smith v. City of Jackson*—Does Disparate Impact Apply in Age Bias Cases?

In *Smith v. City of Jackson*,⁷ the Court held (5–3, with O'Connor concurring in the judgment, but essentially dissenting) that the federal

6. *Stenberg v. Carhart*, 530 U.S. 914 (2000).

7. 125 S. Ct. 1536 (2005).

Age Discrimination in Employment Act (ADEA)⁸ authorizes disparate-impact challenges.⁹ However, because the ADEA has a provision permitting “otherwise prohibited” differentiation based on a “reasonable factor other than age,” plaintiffs still lost.¹⁰ (As I told my colleague Glen Nager, who argued the case for the respondent, he “really” won.)

In order to retain younger personnel and rationalize its pay structure, the City of Jackson, Mississippi granted pay raises to all police officers and dispatchers, thus matching their compensation to the regional average.¹¹ The raises were proportionally greater for officers with less than five years of service than for those who had more seniority.¹² Since most of the officers over 40 years of age had been on the force longer than five years, a group of older officers sued under the ADEA, arguing that they had a right to recover for this disparate impact under principles akin to those recognized in *Griggs v. Duke Power Co.*¹³ The Court in *Griggs* had ruled unanimously that Title VII of the Civil Rights Act of 1964¹⁴ authorizes disparate-impact suits.¹⁵

Justice Stevens, writing for himself and Justices Souter, Ginsberg and Breyer (what I have affectionately termed “the gang of four”), held that the ADEA had to be read in line with the interpretation given Title VII in *Griggs*.¹⁶ In *Griggs*, relief was permitted under the language of section 703(a)(2) of Title VII, and since the language of that section was virtually identical to the language of section 4(a)(2) of the ADEA, the *Smith* Court held that the disparate-impact theory had to be extended to ADEA claims as well.¹⁷

Candor may require acknowledgment that the Court in *Griggs* did not spend very much time parsing the language of section 703(a)(2). The case was decided more as a matter of underlying policy—whether employers should be able to replicate the effects of prior discrimination by using ostensibly “neutral” devices like high school diploma requirements and aptitude test scores—than statutory language. Yet, with over hundreds of cases in the lower courts and nearly a dozen Supreme Court decisions working out the further reaches of disparate impact, the claim of stare decisis was quite strong.

Title VII was amended in 1991 to modify the Court’s holding in *Ward’s Cove Packing Co. v. Atonio*.¹⁸ In that case, the Court tried to

8. 29 U.S.C. § 621 *et seq.*

9. *Smith*, 125 S. Ct. at 1544.

10. *Id.* at 1546.

11. *Id.* at 1539.

12. *Id.*

13. 401 U.S. 424 (1971).

14. 42 U.S.C. § 2000e *et seq.*

15. *Griggs*, 401 U.S. at 436.

16. *Smith*, 125 S. Ct. at 1544.

17. *Id.* at 1542–43.

18. 490 U.S. 642 (1989).

limit the scope of disparate-impact liability; that aspect of *Ward's Cove* was overturned in the 1991 amendments.¹⁹ The 1991 law, however, did not amend the ADEA in this regard, and thus the *Smith* Court (Justice Scalia joined this part) reasoned that “*Ward's Cove's* pre-1991 interpretation of Title VII's identical language remains applicable to the ADEA.”²⁰ The aspect of *Ward's Cove* that seems to have survived is the insistence that the plaintiff is “responsible for isolating and identifying the *specific* employment practices that are allegedly responsible for any observed statistical disparities.”²¹ Plaintiffs in *Smith* were faulted for failing to identify such a practice with sufficient specificity.²²

The ADEA also differs from Title VII in that it includes a provision, Section 4(f)(1), that allows employers to take any action otherwise prohibited under subsection (a) of the act, if the differentiation is based on “reasonable factors other than age discrimination” (the RFOA provision).²³ This section, the *Smith* plurality notes, privileges a broader range of employer justifications than the “business necessity” test under Title VII.²⁴ As Justice Stevens' opinion notes with respect to the City of Jackson's pay policy,

[w]hile there may have been other reasonable ways for the City to achieve its goals, the one selected was not unreasonable. Unlike the business necessity test, which asks whether there are other ways for the employer to achieve its goals that do not result in a disparate impact on a protected class, the reasonableness inquiry includes no such requirement.²⁵

These differences—the fact that ADEA's disparate-impact approach was not the subject of the 1991 amendments and the availability of the RFOA defense—function to allow a more limited liability theory than the one *Griggs* found in Title VII, while still allowing the Court to hold that structural similarity in the language of the two statutes requires that disparate impact challenges be available in theory.

Justice Scalia, interestingly, opted to concur on the basis of deference to administrative agency interpretations under *Chevron U.S.A. Inc. v. National Resources Defense Council, Inc.*,²⁶ even though the agency he was deferring to in this case was the Equal Employment Opportunity Commission (EEOC).²⁷ While the EEOC probably isn't a favorite agency of political conservatives, this approach offered a rather elegant solution from Scalia's perspective. Although in all likelihood he

19. *Id.* at 656–57.

20. *Smith*, 125 S. Ct. at 1545.

21. *Ward's Cove Packing Co.*, 490 U.S. at 656 (emphasis added).

22. *Smith*, 125 S. Ct. at 1545.

23. *Id.* at 1543.

24. *Id.* at 1546.

25. *Id.*

26. 467 U.S. 837, 843–44 (1984).

27. *Smith*, 125 S. Ct. at 1546 (Scalia, J., dissenting).

would not have agreed with the decision in *Griggs* had he been on the Court when it was decided, the case has been settled precedent for decades, and the justices, liberal and conservative alike, were disinclined to disturb it. However, as a diagnosed and documented “textualist,” Scalia would have had difficulty aligning with the plurality in reading into the ADEA anything he could not find evident from the statutory language in either Title VII or ADEA. The EEOC’s regulation permitted him to concur in the Court’s decision while remaining faithful to his judicial philosophy for interpreting statutes.

Justice O’Connor, in her opinion concurring in the judgment that was joined by Justices Kennedy and Thomas, argued that disparate impact could not be read into the ADEA, noting that *Griggs* had not been decided when the ADEA was enacted.²⁸ While the language was parallel, there was no clear intent to authorize disparate-impact claims in ADEA. Rather, Title VII, unlike ADEA, could best be understood as a decision dealing with the “qualitatively different” problem of racial discrimination; *Griggs* “was not based on any analysis of Title VII’s actual language. Rather, the *ratio decidendi* was the statute’s perceived purpose . . .”²⁹ O’Connor disagreed with Scalia’s administrative deference as well, noting that it was not an appropriate application of *Chevron*, because the EEOC’s views were set forth more as an explanation of enforcement objectives rather than a binding interpretation of the statutory reach intended to have “the requisite ‘force of law.’”³⁰

Although all the judges concurred in the outcome, there were significant disagreements under the surface. The liberal justices reaffirmed *Griggs* by holding that the language in the ADEA must serve the same purpose as the virtually identical language in Title VII, while Scalia implicitly criticized *Griggs* by refusing to marry his vote on the outcome in *Smith to Griggs*’ logic. O’Connor openly disagreed with the *Griggs* Court’s statutory analysis, declining to read or infer something into the statute (or the ADEA) that she did not believe was there.

B. *Jackson v. Birmingham Board of Education—Does Title IX Impliedly Authorize Retaliation Claims?*

In *Jackson v. Birmingham Board of Education*, Justice O’Connor joined the liberal group and wrote the 5–4 opinion for the Court.³¹ The question was whether Title IX of the Education Amendments of 1972’s³² protection against sex discrimination by recipients of federal financial assistance applies to retaliation by indirect-victim third parties for reporting prohibited discrimination.³³

28. *Smith*, 125 S. Ct. at 1557 (O’Connor, J., concurring).

29. *Id.* at 1552, 1557.

30. *Id.* at 1558.

31. *Jackson v. Birmingham Bd. of Educ.*, 125 S. Ct. 1497, 1502 (2005).

32. Pub. L. No. 92-318, 86 Stat. 373, as amended, 20 U.S.C. § 1681 *et seq.*

33. *Jackson*, 125 S. Ct. at 1502.

A male physical education teacher and coach of the girls' basketball team at a Birmingham, Alabama high school began complaining that his team was not receiving equal resources.³⁴ As a result, he was given negative performance evaluations and was removed from his position as coach.³⁵ He sued, charging that he had been retaliated against for attempting to redress discriminatory conduct under Title IX.³⁶ The Supreme Court held that Title IX provides a cause of action on these facts.³⁷

Does the Title IX prohibition of "discrimination . . . on the basis of sex" impliedly also protect against retaliation for reporting sex discrimination?³⁸ The liberal justices, favoring a muscular, "progressive" jurisprudence, pushed for a broad interpretation of "discrimination" under Title IX, while the conservatives sought to limit the reach of the term, restricting Title IX's implied right of action to direct victims of direct discrimination in federally funded programs.

For Justice O'Connor and the liberal group, this case rested on considerations of stare decisis, stemming both from the Court's string of decisions extending Title IX's implied right of suit and from the 1969 decision in *Sullivan v. Little Hunting Park, Inc.*,³⁹ awareness of which could be attributed to Congress when it enacted Title IX in 1972.⁴⁰ In *Sullivan*, a white man had rented a house to a black man and assigned him a membership share and rights to use a private park.⁴¹ The corporation that owned the park would not approve the assignment, and Sullivan was permitted to sue under 42 U.S.C. § 1982 for retaliation for advocacy of the black lessee's cause.⁴² According to the *Jackson* Court, since this case was decided prior to the passage of Title IX, Congress had ample notice that "discrimination" could be read to include retaliation.⁴³ Thus, the fact that Congress did not list retaliation as a specific discriminatory practice, as it had in the 1964 enactment in Title VII, was held to be no defect in the plaintiff's case.

Justice Thomas, writing for himself, Chief Justice Rehnquist, and Justices Scalia and Kennedy, dissented. They reasoned, in part, that since Title IX imposes obligations on the states through Congress's spending powers, such conditions should be explicit and unambiguous such that recipients are given clear notice of the obligations they are

34. *Id.* at 1503.

35. *Id.*

36. *Id.*

37. *Id.* at 1509–10.

38. 20 U.S.C. § 1681(a).

39. 396 U.S. 229 (1969).

40. *Jackson*, 125 S. Ct. at 1506.

41. *Sullivan*, 396 U.S. at 235.

42. *Id.* at 406.

43. *Jackson*, 125 S. Ct. at 1506.

assuming when accepting federal funding.⁴⁴ Title IX, however, did not contain a sufficiently clear statement that it reached retaliation. *Sullivan* was deemed distinguishable as a Thirteenth Amendment case not raising the same federalism-clear notice concerns as spending power measures.⁴⁵

C. *Spector v. Norwegian Cruise Line Ltd.*—Does the ADA Cover Foreign-Flag Cruise Ships?

Spector v. Norwegian Cruise Line Ltd., the other major “labor and employment” (if the phrase is stretched) case of the term, involved the question of whether Title III, the public accommodations title, of the Americans with Disabilities Act of 1990 (ADA)⁴⁶ applies to foreign-flag cruise ships.⁴⁷ The petitioners were a class of passengers with disabilities who allegedly had not been accommodated by the respondent cruise line.⁴⁸ The Court split off into a number of opinions; Justice Kennedy authored the lead opinion.

This case presented a fairly narrow question of statutory interpretation but one of crucial interest to the foreign-flag cruise ship industry. Presumably, the ADA could be rather easily read to include cruise ships as covered places of public accommodation. The question for the Court was whether applying the ADA to foreign-flag ships triggered concerns over extraterritorial application of U.S. statutes requiring an especially “clear statement” from Congress that it intended the ADA to have such a reach.

Justice Kennedy, writing for the Court in part and a plurality in part, held that the ADA applied—some of the time.⁴⁹ Foreign-flag ships were not, without specific evidence of congressional intent, subject to U.S. laws that governed the “internal order” of the ship, such as the relations between the captain and its crew, but were reached by laws that governed “the peace of the port.”⁵⁰ The Court had held in *Benz v. Compania Naviera Hidalgo*⁵¹ that the National Labor Relations Act (NLRA) was inapplicable to the foreign crew of a foreign vessel because it was an “internal-order” regulation.⁵² However, the NLRA was fully applicable to a foreign ship’s port-side relations with American longshoremen in *Longshoremen v. Ariadne Shipping Co.*, as that was a “peace of the port” application of the NLRA.⁵³

44. *Id.* at 1510 (Thomas, J., dissenting).

45. *Id.* at 1516.

46. 42 U.S.C. § 12181 *et seq.*

47. *Spector v. Norwegian Cruise Line Ltd.*, 125 S. Ct. 2169, 2174 (2005).

48. *Id.* at 2175.

49. *Id.* at 2184.

50. *Id.* at 2177.

51. 353 U.S. 138 (1957).

52. *Id.*

53. 397 U.S. 195, 200 (1970).

Justice Kennedy argued that the relations between a foreign-flag cruise company and U.S. passengers did not impinge upon the internal order of the ship, and Congress could regulate the treatment of disabled U.S. passengers.⁵⁴ There was one important caveat to the ruling: To the extent the ADA required structural modifications of ships that conflicted with international legal obligations or endangered the crew or passengers, the Court left open the possibility that the ADA would not authorize such modifications or that an “internal affairs clear statement rule” would be triggered requiring more explicit authorization from Congress.⁵⁵

Justice Scalia, joined this time by O'Connor and Rehnquist, dissented. He argued that requiring ships to comply with the ADA necessarily implicated the internal order of the ship, and interfered with other laws.⁵⁶ Safety, he noted, was typically governed, as a matter of internal order, by the laws of the flag state; the strictures of the U.S. law, while perhaps satisfying most domestic safety laws, could conflict with foreign law or treaties.⁵⁷ The fundamental design changes the plaintiffs demanded—accessible staterooms, public restrooms, and wheelchair-accessible cabins—all implicated the physical structure of the ship, its operation at sea, and hence its “internal affairs,” requiring a clear statement from Congress absent in Title III of the ADA.⁵⁸

D. *Remnants of the Term*

Other labor and employment cases include—

- *Commissioner v. Banks*⁵⁹—a unanimous holding that a discrimination plaintiff whose recovery constitutes income must report as gross income the contingent fee paid to his attorney (for clients, “the deepest cut of all”).⁶⁰ This ruling is mitigated by the Civil Rights Tax Relief Act, part of the American Jobs Creation Act of 2004, which provides that attorney fees paid by or on behalf of a taxpayer in connection with discrimination claims will be treated as an “above the line” item and not subject to the limitation on itemized deductions.⁶¹
- *Rousey v. Jacoway*⁶²—a unanimous holding that assets in an individual retirement account (IRA) can be exempted from the bankruptcy estate because they involve a right to payment “on account of . . . age” within the meaning of section 522(d)(10)(E)

54. *Spector*, 125 S. Ct. at 2181.

55. *Id.*

56. *Id.* at 2189–90 (Scalia, J., dissenting).

57. *Id.* at 2189.

58. *Id.*

59. 124 S. Ct. 826 (2005).

60. *Id.* at 829.

61. See 26 U.S.C. § 62(a)(19).

62. 125 S. Ct. 1561 (2005).

of the Bankruptcy Code, even though plan participants can withdraw the balance before age 59½ but subject to a 10 percent penalty.⁶³ A ruling going the other way would have been a trap for the unwary because of the common practice of rolling over distributions from pension plans into IRAs.

- *City of San Diego v. Roe*⁶⁴—a unanimous holding sustaining discharge of a police officer who made and sold explicit sex videos that showed him in a police uniform while off duty.⁶⁵
- *Stewart v. Dutra*⁶⁶—a unanimous ruling that a dredge is a “vessel” under the Longshoremen’s workers compensation and the Jones Act.⁶⁷

E. *Cases on the Horizon*

The Court already has granted review in a number of labor and employment cases scheduled for argument in the fall.

In *Tum v. Barber Foods*⁶⁸ and *Alvarez v. IBP, Inc.*,⁶⁹ the Court will consider the question of whether walking and waiting time associated with the donning and doffing of required safety equipment is compensable under the Fair Labor Standards Act of 1938, as amended by the Portal-to-Portal Act of 1949.⁷⁰ The time periods in question are relatively short when considered on a per-employee basis. However, aggregated over a large number of employees and assessed retroactively over a period of years, the damages faced by these defendants could be quite significant.⁷¹

Another case, *Arbaugh v. Y&H Corp.*, deals with the question of whether Title VII’s fifteen-employee coverage threshold, 42 U.S.C. § 2000e(b), is a nonwaivable jurisdictional requirement.⁷²

In *Garcetti v. Ceballos*, the Court will decide whether the First Amendment protects a deputy district attorney who wrote a memorandum to his supervisor alleging that the deputy sheriff lied on a search

63. *Id.* at 1564.

64. 125 S. Ct. 521 (2004).

65. *Id.* at 524.

66. 125 S. Ct. 1118, 1121 (2005).

67. Although not technically a labor and employment decision, *MGM v. Grokster* 125 S. Ct. 2764 (2005), is of interest. Justice Souter’s opinion states: “We hold that one who distributes a device with the object of promoting its use to infringe copyright, as shown by clear expression or other affirmative steps to foster infringement, is liable for the resulting acts of infringement by third parties.” *Id.* at 2770.

68. 360 F.3d 274 (1st Cir. 2004), *cert. granted*, No. 04-66.

69. 339 F.3d 894 (9th Cir. 2003), *cert. granted*, No. 03-1238.

70. *Tum*, 360 F.3d at 274, *cert. granted*, No. 04-66; *Alvarez*, 339 F.3d at 894, *cert. granted*, No. 03-1238.

71. The author is counsel of record on a brief amici curiae filed on behalf of the U.S. Chamber of Commerce, National Ass’n. of Manufacturers, Society for Human Resources Management, and Association of International Automobile Manufacturers, in support of respondent Barber Foods in the *Tum* case.

72. *Arbaugh v. Y&H Corp.*, 380 F.3d 219 (5th Cir. 2004), *cert. granted*, No. 04-944.

warrant application.⁷³ The issue is whether a purely job-related memorandum on a matter of public concern is protected by the First Amendment.

In *Domino's Pizza v. McDonald*, the question is whether a shareholder can recover under 42 U.S.C. § 1981 for a third party's breach of contract with the corporation.⁷⁴

Schaffer v. Weast raises the question: under the Individuals with Disabilities Education Act, when parents of a disabled child reach an impasse with the school district over the child's individualized education program, which side has the burden of proof in the hearing before the administrative officer?⁷⁵

In *United States v. Olson*, the Court will decide whether inspectors/supervisors for the Mine Safety and Health Administration are immune under the Federal Tort Claims Act for negligence in carrying out or failing to carry out mandatory agency policies and procedures.⁷⁶

In *United States v. Georgia* and *Goodman v. Georgia*, the Court will decide whether Title II of the ADA is a valid exercise of Congress's section 5 enforcement authority under the Fourteenth Amendment, abrogating the states' immunity from damages suits under the Eleventh Amendment, as applied to the administration of prisons.⁷⁷ In *Tennessee v. Lane*, the Court held that Title II as related to "access to legal services" was a valid section 5 enactment.⁷⁸ However, in *Board of Trustees of University of Alabama v. Garrett*, Title I, the employment title of the ADA, was held not to be a valid section 5 measure.⁷⁹

Finally, in *Whitman v. Department of Transportation*, the Court will decide whether the Civil Service Reform Act's provision stating that collectively bargained grievance procedures are the exclusive means of resolving employee grievances precludes judicial review of federal employees' statutory and constitutional claims.⁸⁰

III. Conclusion

The Court's labor and employment docket is not as large as it has been in past years, but significant cases involving the workplace continue to require the Court's attention. All eyes are, of course, on Chief Justice Roberts.

73. *Garcetti v. Ceballos*, 361 F.3d 1168 (9th Cir. 2004), *cert. granted*, No. 04-473.

74. *Domino's Pizza v. McDonald*, No. 02-16900, slip op. (9th Cir. June 18, 2004), *cert. granted*, No. 04-593.

75. *Schaffer v. Weast*, 377 F.3d 449 (4th Cir. 2004), *cert. granted*, No. 04-698.

76. *United States v. Olson*, 362 F.3d 1236 (9th Cir. 2004), *cert. granted*, No. 04-759.

77. *United States v. Georgia*, *Goodman v. Georgia*, No. 02-10168, slip op. (11th Cir. Sept. 16, 2004), *cert. granted*, No. 04-1236; *cert. granted*, No. 04-1203.

78. *Tennessee v. Lane*, 541 U.S. 509, 534 (2004).

79. *Bd. of Tr. of Univ. of Alabama v. Garrett*, 513 U.S. 356, 374 (2001).

80. *Whitman v. Dep't of Transp.*, 382 F.3d 938 (9th Cir. 2004), *cert. granted*, No. 04-113.

The Expanding Rights of Transsexuals in the Workplace

Neil Dishman*

I. Introduction

Suppose that you are an attorney representing a locally owned hardware store. You field a call from the store's owner, who tells you that today one of his longtime front-counter employees, a male named Ron, arrived at work clad in high heels, pantyhose, a pink dress, makeup, and hoop earrings. Upon the stunned reactions of his co-workers, Ron explained to everyone within earshot that he has felt like a woman trapped in a man's body since his early childhood, that his psychologist has diagnosed him as a transsexual, that he will be living as a woman from now on, and that he will eventually undergo sex-change surgery. Ron also announced that his new name is "Rhonda" and that he will be using the women's restroom from now on, which the store's female employees are not too happy about. Ron/Rhonda's male co-workers are already beginning to privately snicker and crack lewd jokes, and the store's regular customers are, not surprisingly, rather shocked to see Ron/Rhonda's familiar face adorned with lip gloss and mascara.

The owner vehemently insists that Ron/Rhonda is disrupting his store's operations and must be fired. Would you know how to advise him? Would you even know where to begin?

This article addresses a legal question that is, at times, as awkward and confusing as the sight of a male co-worker wearing a dress: does the law protect transsexuals like Ron/Rhonda from employment discrimination? Twenty years ago, that question would have been answered with a resounding "no." Today, the answer is a complicated "maybe."

At first blush, the issue of transsexual employment rights might seem exotic. It is not—the law in this area is undergoing rapid and important changes. In the last few years, five states (California, Maine, Minnesota, New Mexico, and Rhode Island) amended their employment statutes to explicitly include transsexualism (or "gender identity") as a protected class. In 2006, a sixth state (Illinois) will join them, and at

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least three other states (Hawaii, New Jersey, and Vermont) recently considered similar legislation.¹ Meanwhile, after years of resistance, an increasing number of courts now allow transsexuals to maintain claims of sex or disability discrimination under Title VII and other laws. In a landmark case just this year, a transsexual plaintiff claiming sex discrimination under Title VII secured a \$320,511 verdict (not to mention \$553,725 in attorney fees and costs) against her former employer, and successfully defended it on appeal.²

Moreover, transsexualism is more common than many people perceive. An estimated one in 11,900 persons “born male” and one in 30,400 persons “born female” initiate the sex-change process, at least to the point of undergoing hormone therapy.³ A defense attorney might think of it this way: if your clients’ employees total in the thousands, chances are you will eventually need to counsel a client about a transsexual employee’s rights.

In short, practitioners and judges who frequently encounter employment law need to understand this rapidly developing issue. To that end, this article provides a comprehensive guide to the byzantine patchwork of protections afforded to transsexuals in the workplace.⁴ Part II sets forth a working definition of “transsexual,” and Part III examines the growing number of state statutes explicitly forbidding discrimination on the basis of transsexualism or “gender identity.” Part IV reviews transsexuals’ attempts to frame their claims as “sex discrimination” under Title VII and similar state statutes; these claims were once uniformly rejected, but now they enjoy increasing acceptance. Part V deals with transsexual discrimination framed as “disability discrimination,” a theory that is futile under federal law but has been met with mixed success under state civil-rights laws. Part VI briefly looks at two other, less common claims: transsexual discrimination as “sexual orientation

1. Also, many cities and counties have passed similar ordinances. See, e.g., The National Transgender Advocacy Coalition (Nov. 8, 2005), at <http://www.ntac.org>, Transgender Law & Policy Institute (Nov. 8, 2005), at <http://www.transgenderlaw.org> (last modified Oct. 29, 2005).

2. *Barnes v. City of Cincinnati*, 401 F.3d 729, 733 (6th Cir. 2005), *cert denied*, ___ S. Ct. ___, 2005 WL 2922504 (Nov. 7, 2005) (No. 05-292).

3. Phyllis Randolph Frye & Katrina C. Rose, *Responsible Representation of Your First Transgendered Client*, 66 TEX. B. J. 558, 558 n.1 (July 2003) (citing JOANNE MEYEROWITZ, *HOW SEX CHANGED—A HISTORY OF TRANSEXUALITY IN THE UNITED STATES* 9 (2002)) [hereinafter Frye & Rose].

4. This article does not advocate for or against transsexual rights, nor does it attempt to judge the wisdom of the statutes and cases described *infra*. Those endeavors have already been undertaken by others. See, e.g., Laura Grenfell, *Embracing Law’s Categories: Anti-Discrimination Laws and Transgenderism*, 15 YALE J.L. & FEMINISM 51 (2003); Marvin Dunson III, *Sex, Gender, and Transgender: The Present and Future of Employment Discrimination Law*, 22 BERKELEY J. EMP. & LAB. L. 465 (2001); Jennifer L. Levi, *Paving the Road: A Charles Hamilton Houston Approach to Securing Trans Rights*, 7 WM. & MARY J. WOMEN & L. 5 (2000). Rather, the purpose here is to provide a practical resource for those who litigate and decide cases in this complex area of law.

discrimination” or “appearance discrimination” under state law. Finally, Part VII provides a concise checklist for navigating this maze of federal and state authorities.

II. What a Transsexual Is (and is not)

Strictly speaking, a “transsexual” is a person who is (or could be) diagnosed with a recognized medical condition known as Gender Identity Disorder (sometimes called GID or “gender dysphoria”).⁵ GID is marked by two characteristics: (1) “a strong and persistent cross-gender identification, which is the desire to be, or the insistence that one is, of the other sex”; and (2) “persistent discomfort about one’s assigned sex or a sense of inappropriateness in the gender role of that sex.”⁶ In short, a transsexual is the psyche of a man trapped in the body of a woman, or vice versa.

Transsexualism generally appears at an early age, and it is “incurable,” in the sense that counseling will not relieve transsexuals of their desire to be of the opposite sex.⁷ Rather, the accepted treatment is a gradual transition from the patient’s birth sex to the desired sex. After initial diagnosis, the transsexual must first undergo a “real life” test where he or she assumes the social role of the opposite sex at all times.⁸ In addition to dressing as the opposite sex during this period, the transsexual will usually also begin altering his or her appearance through hormone therapy and, for males, electrolysis.⁹ The transsexual must successfully live as the opposite sex for six months to two years, and only then, upon permission from two treating psychologists, can he or she undergo irreversible surgery to acquire the genitalia of the opposite sex.¹⁰

The term “transsexual” should be distinguished from “transvestite,” “intersexed,” and “transgender.”¹¹ A transvestite (or “cross-dresser”) is a person, generally a heterosexual male, who dresses as the opposite sex purely for sexual excitement; though transvestites and transsexuals both cross-dress, transvestites are content with their birth sex.¹² An

5. *E.g.*, *Lie v. Sky Publ’g Corp.*, 2002 WL 31492397, *1–2 (Mass. Super. Ct. Oct. 7, 2002).

6. AM. PSYCHIATRIC ASS’N, DIAGNOSTIC AND STATISTICAL MANUAL OF MENTAL DISORDERS 576 (4th ed., Text Revision 2000) [hereinafter DSM-IV].

7. *Employment Handicap Discrimination Based on Gender Dysphoria (Transsexualism)*, 25 AM. JUR. 3D. *Proof of Facts* 415 § 1 (2005) [hereinafter *Proof of Facts*]; see DSM-IV, *supra* note 6, at 576–77.

8. *Proof of Facts* 415, *supra* note 7, at § 1.

9. *Id.* Unsurprisingly, “[i]f the transsexual will become a victim of employment discrimination, this is the time when it almost invariably begins.” *Id.*

10. *Id.*

11. *See, e.g.*, *Ulane v. E. Airlines, Inc.*, 742 F.2d 1081, 1083 n.3 (7th Cir. 1984); Frye & Rose, *supra* note 4, at 558–59.

12. *Id.* Similarly, although homosexuals and pre-operative transsexuals share a common trait (attraction to those of the same sex), homosexuals are distinguishable because they do not wish to become a member of the opposite sex. *Id.*

“intersexed” person (sometimes called the now-disfavored term “hermaphrodite”) is someone whose genitalia or chromosomes are ambiguous; unlike a transsexual, an intersexual’s gender confusion comes from a physical, not psychological, condition.¹³ Finally, “transgender” or “transgendered” is an umbrella term encompassing anyone who is “at odds with ‘traditional’ concepts of gender,” whether transsexual, transvestite, intersexed, or otherwise.¹⁴

By necessity, this article focuses mostly on transsexuals, as virtually all of the relevant case law involves plaintiffs who are (or at least claim to be) transsexuals. However, that does not imply that the authorities discussed below could not be read broadly enough to apply to other transgender plaintiffs—it means only that this article focuses on what the law *is*, not on what it might or should *become*.

With these definitions in mind, the following sections examine the intricate patchwork of legal protections for transsexuals in the workplace.

III. State Laws Expressly Forbidding Transsexual Discrimination

In five states—California, Maine, Minnesota, New Mexico, and Rhode Island—the legal status of transsexuals in the workplace is in no doubt. All five have, more or less, added transsexualism as a protected class under their civil-rights statutes.

Minnesota was the first state to take the leap, and it did so in a unique way. Minnesota is one of the handful of states that forbids discrimination based on sexual orientation,¹⁵ and it was the first one to define sexual orientation in a way that expressly covers transsexualism. Specifically, “sexual orientation” includes “having or being perceived as having a self-image or identity not traditionally associated with one’s biological maleness or femaleness.”¹⁶

There are few reported decisions under this law, but one Minnesota Supreme Court case, *Goins v. West Group*,¹⁷ merits discussion. Julianne Goins was born male, but in 1994 she¹⁸ began taking female hormones and presenting herself as a female, and in 1995 she successfully petitioned a court to change her legal name and gender.¹⁹ After she began

13. *Id.* See also DSM-IV, *supra* note 6, at 581.

14. Frye & Rose, *supra* note 4, at 558.

15. MINN. STAT. § 363A.08(2) (2004).

16. *Id.* at § 363A.03(44).

17. *Goins v. W. Group*, 635 N.W.2d 717 (Minn. 2001).

18. After the fashion of nearly every court to consider transsexual claims, this article refers to transsexuals using the pronouns of their desired sex, regardless of their physical condition. See, e.g., *Goins*, 635 N.W.2d at 721. Thus, a male-to-female transsexual is called “she” and “her,” even if she still possesses male genitalia or other male attributes. *Id.* at 721 n.1 (“Because Goins refers to herself as female, we will refer to her in this opinion using feminine pronouns.”).

19. *Id.* at 720–21.

employment with West Group in 1997, her use of the women's restroom drew complaints from female employees; West treated these complaints "as a hostile work environment concern" and directed Goins to use a single-occupancy restroom on a different floor from her office.²⁰ She refused, and after West threatened her with discipline, she resigned.²¹

Goins claimed, *inter alia*, that West's restroom policy was direct evidence of sexual-orientation discrimination. She argued that Minnesota law "prohibits West's policy of designating restroom use according to biological gender, and requires instead that such designation be based on self-image of gender."²² The Supreme Court of Minnesota disagreed, in rather conclusory fashion. The court feared that accepting Goins's claim "would likely restrain employer discretion in the gender designation of workplace shower and locker room facilities, a result not likely intended by the legislature."²³ The court instead held (citing only an opinion of the Minnesota Department of Human Rights) that Minnesota law "neither requires nor prohibits restroom designation according to self-image of gender or according to biological gender," and thus denied Goins's claim.²⁴

In contrast to Minnesota, which includes transsexualism in its definition of "sexual orientation," California considers transsexual discrimination an express form of "sex discrimination." Under California's employment laws, "sex" is defined to include "a person's gender,"²⁵ which is in turn defined to include "a person's gender identity and gender related appearance and behavior whether or not stereotypically associated with the person's assigned sex at birth."²⁶ The laws of New Mexico and Rhode Island take another approach; both make "gender identity" a protected class of its own.²⁷ Both states define the term quite

20. *Id.* at 721.

21. *Id.*

22. *Id.* at 723.

23. *Id.*

24. *Id.* Though this article generally avoids opining on the persuasiveness of the decisions it cites, *Goins* is hard not to criticize. See *supra* note 4. The court cited no authority for its speculative assertion that the legislature did not intend to disturb "the traditional and accepted practice" of designated restrooms, showers, and locker rooms by biological gender. See *Goins*, 635 N.W.2d at 723. Indeed, the court's conclusion that Minnesota law does not "prohibit restroom designation . . . according to biological gender" is difficult to square with the legislature's express prohibition of discrimination against those "having . . . a self-image . . . not traditionally associated with [their] biological maleness or femaleness." *Id.* See also MINN. STAT. § 363A.03(44).

In short, although the Supreme Court of Minnesota has adopted a pinched reading of its transsexualism statute, the *Goins* analysis is weak enough that other states with such statutes might reject it and read their own statutes more broadly. *Goins*, 635 N.W.2d at 723.

25. CAL. GOV'T CODE § 12926(p) (West 2003).

26. CAL. PENAL CODE § 422.56(c) (West 2005).

27. N.M. STAT. ANN. § 28-1-7(A) (Michie 1978) ("gender identity"); R.I. GEN. LAWS § 28-5-8(1)(I) (1956) ("gender identity or expression").

broadly.²⁸ Maine recently followed Minnesota's lead by including "gender identity or expression" in the definition of "sexual orientation."²⁹ On January 1, 2006, Illinois will become the sixth state to protect transsexuals; it recently passed a human-rights bill that mimics Minnesota's and Maine's, by defining "sexual orientation" to include "gender-related identity, whether or not traditionally associated with the person's designated sex at birth."³⁰ And three other states—Hawaii, New Jersey, and Vermont—are either currently considering or recently considered similar legislation.³¹

In sum, express state protections for transsexuals in the workplace are proliferating. At the beginning of 2005, only four states had such laws, but two more states have joined them, and three others have at least thought about it. Also, many cities and counties have written similar protections into their ordinances.³² While there has been little litigation under these laws to date,³³ employees, employers, and practitioners should be aware of them, as they are rapidly creating new

28. See N.M. STAT. ANN. § 28-1-2(Q) ("a person's self-perception, or perception of that person by another, of the person's identity as a male or female based upon the person's appearance, behavior or physical characteristics that are in accord with or opposed to the person's physical anatomy, chromosomal sex or sex at birth"); R.I. GEN. LAWS § 28-5-6(10) ("a person's actual or perceived gender, as well as a person's gender identity, gender-related self image, gender-related appearance, or gender-related expression; whether or not that gender identity, gender-related self image, gender-related appearance, or gender-related expression is different from that traditionally associated with the person's sex at birth").

29. 2005 Me. Legis. Serv. Ch. 10 (S.P. 413) (L.D. 1196) (West). The law, which was approved on March 31, 2005, does not further define "gender identity or expression."

30. 2003 Ill. Laws 1078, at *5. This legislation was approved on January 21, 2005, and becomes effective on January 1, 2006. *Id.*

31. Hawaii's bill would have added "gender identity" as a protected class and borrowed Rhode Island's definition of the term. See *supra* note 28; H.B. 1450, 23rd State Leg. (Haw. 2005), available at <http://www.capitol.hawaii.gov/site1/docs/getstatus.asp?qu=hb+1450&showstatus=on&press1=docs>. It was passed by both houses of the legislature but was recently vetoed by the governor. *Id.*

New Jersey's bills would add "gender identity or expression" as a protected class, defined as "having or being perceived as having a gender related identity or expression whether or not stereotypically associated with a person's assigned sex at birth." S.B. No. 2437, 211th Legislature, 2d Reg. Sess. (N.J. 2004); A.B. No. 3678, 211th Legislature, 2d Reg. Sess. (N.J. 2004), available at <http://www.njleg.state.nj.us/bills/BillsByNumber.asp>. Identical bills have been introduced and referred to each chamber's respective Judiciary Committee. *Id.*

Vermont's bill would add "gender identity or expression" as a protected class, without defining the term. N.B. No. 478, 68th Biennial Sess. (Vt. 2005), available at <http://www.leg.state.vt.us/database/status.cfm>. The bill has been introduced and referred to the House Judiciary Committee. *Id.*

32. Complete lists of such ordinances are maintained by transgender advocacy groups. See, e.g., *U.S. Jurisdictions with Laws Prohibiting Discrimination on the Basis of Gender Identity or Expression*, at <http://www.transgenderlaw.org/ndlaws/index.htm#jurisdictions>.

33. Perhaps surprisingly, there are no reported cases invoking California, Maine, New Mexico, or Rhode Island's prohibitions on transsexual discrimination.

workplace rights for a class of people that had no such rights anywhere in the country just a few years ago.

Against this backdrop, the next section discusses an issue that, in contrast, has been extensively litigated: whether transsexual discrimination constitutes sex discrimination.

IV. Do Federal and State Sex-Discrimination Laws Protect Transsexuals?

Title VII of the Civil Rights Act of 1964 prohibits employers from discriminating “because of . . . sex,”³⁴ and for almost thirty years,³⁵ transsexual plaintiffs have been imploring courts to apply this provision to them. While the courts originally refused, the trend may now be moving in the other direction.

A. Initial Denial of Transsexual Title VII Claims

The first courts to consider the issue uniformly rejected transsexuals’ Title VII claims. The seminal case is the Seventh Circuit’s 1984 decision in *Ulane v. Eastern Airlines, Inc.*³⁶ Kenneth Ulane was born male and hired by Eastern Airlines as a pilot; eleven years later, she was diagnosed as a transsexual.³⁷ She underwent hormone therapy and sex-reassignment surgery, obtained a revised birth certificate, and had the FAA recertify her flight status as a female.³⁸ When she returned to work after her surgery, Eastern learned for the first time that she was a transsexual and fired her.³⁹ Ulane sued, claiming that she had been discriminated against both “as a transsexual” and “as a female.”⁴⁰

The Seventh Circuit rejected both of Ulane’s claims. In regards to Ulane’s claim of discrimination “as a transsexual,” the court unequivocally held that “Title VII does not protect transsexuals.”⁴¹ The court first argued that the word “sex” in Title VII forbids discrimination “against women because they are women and against men because they are men”—not “against a person who has a sexual identity disorder . . . or discontent with the sex into which they were born.”⁴² The court found no legislative history suggesting that “sex” should be interpreted to encompass transsexuals, and it also argued that Congress’s repeated refusal to add sexual orientation to Title VII’s protected classes, while not directly analogous to the transsexual question, lent further support

34. 42 U.S.C. § 2000e-2(a)(1) (2005).

35. See, e.g., *Holloway v. Arthur Andersen & Co.*, 566 F.2d 659, 661–62 (9th Cir. 1977).

36. 742 F.2d 1081 (7th Cir. 1984).

37. *Id.* at 1082–83.

38. *Id.*

39. *Id.*

40. *Id.* at 1082.

41. *Id.* at 1084.

42. *Id.* at 1085.

to a “narrow, traditional interpretation” of the word “sex.”⁴³ Therefore, the court refused to “judicially expand the definition of sex” to include transsexuals.⁴⁴

The court also made short work of Ulane’s second claim, discrimination “as a female.” Although the court entertained the idea that Ulane might be legally considered a female and thus enjoy Title VII’s protections on that basis, it did not need to resolve the question, as it concluded that there was no evidence of sex discrimination.⁴⁵ Rather, the court found that “if Eastern did discriminate against Ulane, it was not because she is a female, but because Ulane is a transsexual—a biological male who takes female hormones, cross-dresses, and has surgically altered parts of her body to make it appear to be female.”⁴⁶ Since the court had already determined that Title VII does not prohibit discrimination against transsexuals because they are transsexual, it concluded that Ulane had no viable Title VII claim.⁴⁷

During roughly the same time period as *Ulane*, two other federal circuits came to similar conclusions. In *Holloway v. Arthur Andersen & Company*,⁴⁸ the Ninth Circuit ruled that “an employee may be discharged, consistent with Title VII, for initiating the process of sex transformation.”⁴⁹ The court reached this result by adopting the traditional definition of “sex” as “based on anatomical characteristics” and rejecting the plaintiff’s suggestion that “sex” includes the looser concept of “gender,” which “would encompass transsexuals.”⁵⁰ In short, the court held that Title VII is meant “to ensure that men and women are treated equally,” and no more.⁵¹ And in *Sommers v. Budget Marketing, Inc.*,⁵² the Eighth Circuit similarly opined that “sex” refers to “anatomical classifications,” not to an individual’s “psychological makeup”; thus, it flatly held that Title VII does not protect transsexuals from discrimination.⁵³

B. *Sex Stereotyping and Price Waterhouse: The Tide Turns?*

By the late 1980s, every federal court to consider the issue had ruled that discrimination against transsexuals does not qualify as sex discrimination under Title VII. But in 1989, the Supreme Court cast doubt on these precedents, perhaps unintentionally, when it decided *Price Waterhouse v. Hopkins*.⁵⁴ Although *Price Waterhouse* did not in-

43. *Id.* at 1085–86.

44. *Id.* at 1086.

45. *Id.* at 1087.

46. *Id.*

47. *Id.*

48. *See generally Holloway*, 566 F.2d at 659.

49. *Id.* at 661.

50. *Id.* at 662–63.

51. *Id.* at 663.

52. *See generally* 667 F.2d 748 (8th Cir. 1982).

53. *Id.* at 749–50.

54. *See generally* 490 U.S. 228 (1989).

volve transsexualism (nor even mention it), it nonetheless had potentially sweeping implications for transsexual employment rights.

Price Waterhouse involved a female senior manager, Ann Hopkins, who was denied partnership at Price Waterhouse, a nationwide accounting firm.⁵⁵ Although Hopkins was highly praised by the partners in her office and had recently landed a major contract, she was passed over by the wider partnership (consisting of 655 men and 7 women) because of concerns about her “interpersonal skills.”⁵⁶ As it turned out, this was merely a euphemism, behind which lay hostility towards Hopkins’s perceived masculinity.⁵⁷ In deliberations on her candidacy, partners complained that she was too “macho,” opined that she could use “a course at charm school,” and objected to her frequent use of profanity, to which one partner responded that the objection came only “because it’s a lady using foul language.”⁵⁸ Worst of all, the partner charged with explaining the partnership denial to Hopkins told her she could improve her chances next year if she would just “walk more femininely, talk more femininely, dress more femininely, wear make-up, have her hair styled, and wear jewelry.”⁵⁹

As one small part of its lengthy analysis of the case, the Court announced that such sex stereotyping is actionable under Title VII:

In the specific context of sex stereotyping, an employer who acts on the basis of a belief that a woman cannot be aggressive, or that she must not be, has acted on the basis of gender. Although the parties do not overtly dispute this . . . proposition, the placement by Price Waterhouse of “sex stereotyping” in quotation marks throughout its brief seems to us an insinuation either that such stereotyping was not present in this case or that it lacks legal relevance. We reject both possibilities. . . . As for the legal relevance of sex stereotyping, we are beyond the day when an employer could evaluate employees by assuming or insisting that they matched the stereotype associated with their group.⁶⁰

As another court later summarized, *Price Waterhouse* “held that Title VII barred not just discrimination based on the fact that Hopkins was a woman, but also discrimination based on the fact that she failed to act like a woman.”⁶¹

55. *Id.* at 231–32.

56. *Id.* at 234–35.

57. *Id.* at 235.

58. *Id.*

59. *Id.*

60. *Id.* at 250–51 (internal citation omitted). This holding was announced in Justice Brennan’s plurality opinion on behalf of four Justices and was joined by two concurring Justices. *See id.* at 258–61 (White, J., concurring); *id.* at 272–73 (O’Connor, J., concurring).

61. *Schwenk v. Hartford*, 204 F.3d 1187, 1201 (9th Cir. 2000) (internal quote marks omitted).

While *Price Waterhouse* did not directly address transsexualism, its expansion of the meaning of “sex” under Title VII casts great doubt on the reasoning of the *Ulane* line of cases. Transsexuals, almost by definition, do not “match[] the stereotype associated with their [sex]”;⁶² rather, they adopt the clothing, names, pronouns, hormones, and, eventually, body parts of the opposite sex. Thus, if discrimination for failure to conform to sexual stereotypes violates Title VII, it seems that transsexuals are protected from discrimination after all.⁶³

Yet, for a decade after *Price Waterhouse*, courts (and apparently litigants) did not seem to make the connection between *Price Waterhouse* and transsexuals. In the 1990s, federal district courts continued to reject transsexual Title VII claims with cursory citations to *Ulane* and its kin, and without mentioning *Price Waterhouse*.⁶⁴

That began to change with the Ninth Circuit’s 2000 decision in *Schwenk v. Hartford*.⁶⁵ Douglas Schwenk was born male, but took illegally obtained female hormones, went by the name “Crystal Marie,” and consistently presented herself as a woman.⁶⁶ She became incarcerated in an all-male prison, where she confided in a guard that she was transsexual and intended to eventually have sex-reassignment surgery.⁶⁷ The guard, apparently sexually aroused by this revelation, then subjected her to an extensive campaign of sexual harassment and assault.⁶⁸ At first, his attentions were limited to propositioning Schwenk and making obscene gestures and comments; he later turned to groping her and offering to bring her makeup and “girl stuff” in return for sex, and eventually, he attempted to force oral sex on her and forcibly rubbed his exposed penis against her.⁶⁹ Schwenk later sued the guard and other prison officials under, *inter alia*, the federal Gender Motivated Violence Act (GMVA),⁷⁰ which provides a cause of action for victims of “crime[s] of violence committed because of gender or on the basis of gender, and due, at least in part, to an animus based on the victim’s

62. *Price Waterhouse*, 490 U.S. at 251.

63. Note that *Price Waterhouse* likely does not have a similar effect on homosexuals or bisexuals claiming discrimination. While virtually all transsexuals will eventually take on some characteristics of the opposite sex, not all homosexuals or bisexuals defy gender stereotypes (outside of their choice of sexual partners, which an employer often will not know). Thus, *Price Waterhouse* “would not bootstrap protection for sexual orientation into Title VII.” *Simonton v. Runyon*, 232 F.3d 33, 37–38 (2d Cir. 2000).

64. *Rentos v. Oce-Office Sys.*, 1996 WL 737215, at *7–8 (S.D.N.Y. Dec. 24, 1996); *Dobre v. Nat’l R.R. Passenger Corp.*, 850 F. Supp. 284, 286–87 (E.D. Pa. 1993); *cf.* *James v. Ranch Mart Hardware, Inc.*, 881 F. Supp. 478, 481–82 (D. Kan. 1995) (rejecting claim that defendant fired plaintiff “for being a male transsexual when it would not have fired her for being a female transsexual”).

65. 204 F.3d at 1187 n.4.

66. *Id.* at 1193.

67. *Id.*

68. *Id.* at 1193–94.

69. *Id.*

70. 42 U.S.C. § 13981(c) (2000).

gender.”⁷¹ Legislative history suggests that Title VII’s interpretive principles also should apply to the GMVA, and thus the Ninth Circuit examined Title VII precedents to determine whether the guard’s attacks on Schwenk were “because of gender.”⁷² On this point, the guard argued that (1) the attack occurred because of Schwenk’s transsexuality; (2) transsexuality is a “psychiatric illness” rather than “an element of gender”; and therefore (3) the attack was not “because of gender,” rendering the GMVA inapplicable.⁷³

The court acknowledged that it had previously, in *Holloway*, determined that Title VII does not protect transsexuals, and that other courts had similarly limited Title VII’s protections to “biological or anatomical characteristics” (i.e., “sex”), as opposed to “socially-constructed characteristics” (i.e., “gender”).⁷⁴ However, the court held that *Holloway*, *Ulane*, and their progeny were “overruled by the logic and language of *Price Waterhouse*.”⁷⁵ In the court’s view, *Price Waterhouse* rendered the terms “sex” and “gender” interchangeable under both Title VII and the GMVA, meaning that both statutes now prohibit discrimination for the victim’s failure to conform to “socially-constructed gender expectations.”⁷⁶ And because the guard’s harassment was clearly motivated “by [Schwenk’s] assumption of a feminine rather than a typically masculine appearance or demeanor,” the court concluded that his actions were “because of gender” under the GMVA and allowed Schwenk’s claim to survive summary judgment.⁷⁷

A few months after *Schwenk*, the First Circuit handed down a similar ruling under yet another analogous federal statute. In *Rosa v. Park West Bank and Trust Company*,⁷⁸ Lucas Rosa, a biological male, arrived at a bank dressed in feminine clothing and attempted to apply for a loan.⁷⁹ After examining his identification, which apparently depicted Rosa in masculine attire, a bank employee refused to give him a loan application until he “went home and changed.”⁸⁰ Rosa sued under the Equal Credit Opportunity Act (ECOA),⁸¹ which prohibits, *inter alia*, sex discrimination by potential creditors.⁸² The district court, opining that any discrimination was due to Rosa’s choice of attire, not sex, dismissed Rosa’s case for failure to state a claim.⁸³ But the First Circuit reversed

71. *Id.*

72. *Schwenk*, 204 F.3d at 1200–01.

73. *Id.* at 1200.

74. *Id.* at 1201.

75. *Id.*

76. *Id.* at 1202.

77. *Id.*

78. 214 F.3d 213 (1st Cir. 2000).

79. *Id.* at 214.

80. *Id.*

81. 15 U.S.C. § 1691 *et seq.* (2000).

82. *Rosa*, 214 F.3d at 214.

83. *Id.*

because it believed (applying Title VII principles to the ECOA) that *Price Waterhouse* might make Rosa's claim viable.⁸⁴ The court inferred that the bank might have turned Rosa away "because [it] thought that Rosa's attire did not accord with his male gender"; if so, the court reasoned, this would be evidence of sex discrimination under *Price Waterhouse*.⁸⁵ Thus, like the Ninth Circuit in *Schwenk*, the First Circuit at least implied that transsexuals may have viable sex-discrimination claims under Title VII.

Finally, in 2004, the Sixth Circuit took the final step in this logical progression by applying *Price Waterhouse* directly to a transsexual's employment claim. The case, *Smith v. City of Salem, Ohio*,⁸⁶ involved a biologically male firefighter, Jimmie Smith, who had worked for Salem's fire department for seven years without incident before being diagnosed with GID.⁸⁷ After this diagnosis, Smith began "expressing a more feminine appearance" at work.⁸⁸ Several city officials then began conspiring to have her fired, but Smith caught wind of the plot and threatened to sue.⁸⁹ When the fire chief suspended her four days later for a supposedly unrelated infraction, she made good on the threat by bringing suit under Title VII and *Price Waterhouse*.⁹⁰

The district court granted the city's motion for judgment on the pleadings because in its view, Smith's invocation of *Price Waterhouse* was a subterfuge intended to obscure her "real" claim "based on . . . transsexuality," a claim foreclosed by the *Ulane* line of cases.⁹¹ The Sixth Circuit reversed, holding that *Price Waterhouse* "eviscerated" *Ulane* and its kin.⁹² It first argued that because *Price Waterhouse* forbade employers from, for example, discriminating against females for not wearing dresses, "[i]t follows that employers who discriminate against men because they *do* wear dresses . . . are also engaging in sex discrimination."⁹³ Moreover, in the court's opinion, the district court improperly dodged *Price Waterhouse*'s holding:

Price Waterhouse . . . does not make Title VII protection against sex stereotyping conditional or provide any reason to exclude Title VII coverage for non sex-stereotypical behavior simply because the person is a transsexual. As such, *discrimination against a plaintiff who is transsexual—and therefore fails to act and/or identify with his or her gender—is no different from the discrimination directed against Ann Hopkins in Price Waterhouse, who, in sex-stereotypical terms, did*

84. *Id.* at 215–16.

85. *Id.*

86. *See generally* 378 F.3d 566 (6th Cir. 2004).

87. *Id.* at 568.

88. *Id.*

89. *Id.* at 568–69.

90. *Id.* at 569–70.

91. *Id.* at 571–72.

92. *Id.* at 573.

93. *Id.* at 574 (emphasis in original).

not act like a woman. Sex stereotyping based on a person's gender non-conforming behavior is impermissible discrimination, irrespective of the cause of that behavior; a label, such as "transsexual," is not fatal to a sex discrimination claim where the victim has suffered discrimination because of his or her gender non-conformity.⁹⁴

With this sweeping language, the promise that *Price Waterhouse* holds for transsexual plaintiffs finally came to fruition: in the eyes of at least one federal circuit, discrimination against transsexuals and discrimination "because of . . . sex" are indistinguishable. Should the other federal circuits or the Supreme Court come to agree, transsexuals will enjoy protection from employment discrimination nationwide.⁹⁵

C. *A Note of Dissent*

The inclusion of transsexuals under Title VII is not necessarily inexorable, however. At least two federal district courts have explicitly declined to apply the reasoning of *Price Waterhouse* to transsexuals. In the 2002 case of *Oiler v. Winn-Dixie Louisiana, Inc.*,⁹⁶ the plaintiff was a male by birth who crossdressed in some situations, though always outside of work.⁹⁷ (Confusingly, the court stated that Oiler had been diagnosed with GID but was "not a transsexual," and referred to her as either "transgendered," a "crossdresser," or both.⁹⁸) When Oiler's employer terminated her after learning of her crossdressing, she sued under Title VII in the Eastern District of Louisiana.⁹⁹ In rejecting this

94. *Id.* at 574–75 (emphasis added); see also *Kastl v. Maricopa County Cmty. Coll. Dist.*, 2004 WL 2008954, at *2–3 (D. Ariz. June 3, 2004) (similar holding).

95. *Schwenk, Rosa, and Smith* are the only federal appellate cases to expressly allow transsexual claims under Title VII or analogous laws. See generally *Schwenk*, 204 F.3d at 1187; *Rosa*, 214 F.3d at 213; *Smith*, 378 F.3d at 566. However, two other federal circuits have applied Title VII and *Price Waterhouse* in the related context of protecting "effeminate" men from same-sex sexual harassment. *Bibby v. Phila. Coca Cola Bottling Co.*, 260 F.3d 257, 262–63 (3d Cir. 2001) (holding that same-sex harassment is "because of . . . sex" when "harasser's conduct was motivated by a belief that the victim did not conform to the stereotypes of his or her gender"); *Doe v. City of Belleville, Illinois*, 119 F.3d 563, 580–81 (7th Cir. 1997) ("*Price Waterhouse* . . . makes clear that Title VII does not permit an employee to be treated adversely because his or her appearance or conduct does not conform to stereotypical gender roles"), *vacated and remanded on other grounds*, 523 U.S. 1001 (1998). While these cases did not involve transsexuals, they suggest that these two circuits may be amenable to extending Title VII's protections to transsexuals if the question is presented. See generally *id.* These cases are consistent with the Supreme Court's holding in *Oncale v. Sundowner Offshore Services*, where the Court showed a measure of receptiveness to transsexual claims, albeit indirectly, by unanimously holding that persecution of a male by his male co-workers can be actionable sexual harassment under Title VII. *Oncale v. Sundowner Offshore Servs.*, 523 U.S. 75, 78 (1998). Unlike the appellate courts mentioned above, however, the Court did not rest its decision on (nor even cite) *Price Waterhouse*. See *id.*

Also, at least one federal district court has, in an unpublished opinion, distinguished the *Ulane* line of cases in order to allow a same-sex sexual-harassment claim by a transsexual to go forward. *Cox v. Denny's, Inc.*, 1999 WL 1317785 (M.D. Fla. Dec. 22, 1999).

96. 2002 WL 31098541 (E.D. La. Sept. 16, 2002).

97. *Id.* at *1.

98. *Id.* at *1–2.

99. *Id.* at *2–3.

claim, the court approvingly cited *Ulane* and similar cases, and then distinguished *Price Waterhouse* in a manner that excludes all transsexual plaintiffs from its reach:

[T]he Court finds that this is not a situation where the plaintiff failed to conform to a gender stereotype. Plaintiff was not discharged because he did not act sufficiently masculine. . . . Rather, the plaintiff disguised himself as a person of a different sex and presented himself as a female for stress relief and to express his gender identity. . . . Plaintiff's actions are not akin to the behavior of the plaintiff in *Price Waterhouse*. The plaintiff in that case may not have behaved as the partners thought a woman should have, *but she never pretended to be a man or adopted a masculine persona*. . . . While Title VII's prohibition of discrimination on the basis of sex includes sexual stereotypes, the phrase "sex" has not been interpreted to include sexual identity or gender identity disorders.¹⁰⁰

Thus, in contrast to *Smith's* conclusion that *Price Waterhouse* "eviscerated" *Ulane*, the *Oiler* ruling suggests that *Price Waterhouse* and *Ulane* can coexist. On this view, plaintiffs who have mildly nonstereotypical traits (e.g., women who use profanity) are protected from discrimination under *Price Waterhouse*, but *Ulane* continues to exclude those who fully and intentionally present themselves as the opposite sex (e.g., transsexuals).

A year later, in *Sweet v. Mulberry Lutheran Home*,¹⁰¹ the Southern District of Indiana expressly endorsed the *Oiler* rationale when rejecting a transsexual's Title VII claim.¹⁰² The court also noted that the Seventh Circuit (its parent court) has recently cited *Ulane* with approval, albeit outside the context of transsexualism; this was further reason not to accept the plaintiff's argument that *Price Waterhouse* abrogated *Ulane*.¹⁰³

Thus, although federal courts are increasingly receptive to including transsexuals in Title VII's coverage, not everyone is on board just yet. At least two district courts believe that *Ulane* and its kin survive *Price Waterhouse* and thus continue to bar transsexual sex-discrimination claims.

D. *Relief for Transsexuals Under State Sex-Discrimination Laws*

For transsexual plaintiffs, Title VII is not the only game in town; many states have their own legislation prohibiting sex discrimination,

100. *Id.* at *5–6 (emphasis added).

101. *Sweet v. Mulberry Lutheran Home*, 2003 WL 21525058 (S.D. Ind. June 17, 2003).

102. *Id.* at *3.

103. *Id.* (citing *Spearman v. Ford Motor Co.*, 231 F.3d 1080, 1084 (7th Cir. 2000)); *see also Hamner v. St. Vincent Hosp. & Health Care Ctr., Inc.*, 224 F.3d 701, 704 (7th Cir. 2000) (approvingly citing *Ulane* outside of transsexualism context).

and state courts are not bound to interpret their laws the same way federal courts have interpreted Title VII. Accordingly, some transsexuals have litigated their claims under state law instead of (or in addition to) federal law, with mixed success. Courts in Connecticut, Iowa, Pennsylvania, and the District of Columbia have rejected such claims under their state laws, all citing the *Ulane* line of cases and adopting similar reasoning.¹⁰⁴ Conversely, courts in three states—Massachusetts, New Jersey, and New York—have accepted such claims, the first two by relying on *Price Waterhouse*, *Schwenk*, and *Rosa*,¹⁰⁵ and the third simply because it found *Ulane* unpersuasive.¹⁰⁶

Close examination of these decisions would be redundant here, as they add little theoretically to the federal decisions detailed above. However, litigants should be aware that state law can provide an alternate (or additional) battleground for transsexuals who wish to assert sex-discrimination claims.

Having surveyed federal and state law to explore whether transsexuals can successfully claim sex discrimination, the next section addresses whether transsexuals can fit their employment claims into a different box: disability or handicap discrimination.

V. Do Federal and State Disability-Discrimination Laws Protect Transsexuals?

Recall that a transsexual, strictly speaking, is someone who suffers from a medically recognized mental disorder, namely GID or gender dysphoria. This raises another question for the transsexual plaintiff: does discrimination against a transsexual constitute discrimination on the basis of disability or handicap?

Under federal law, the answer is simple: no. Both the Americans with Disabilities Act and its close cousin, the Rehabilitation Act, expressly exclude transsexuals from their protections. Both provide that “transvestism, transsexualism, . . . [and] gender identity disorders not resulting from physical impairments” are not “disabilities.”¹⁰⁷

Under state disability laws, however, transsexual plaintiffs have achieved mixed results. Courts in two states, Iowa and Pennsylvania, have held that transsexual plaintiffs are not disabled under their

104. *E.g.*, *Underwood v. Archer Mgmt. Serv., Inc.*, 857 F. Supp. 96, 98 (D.D.C. 1994) (interpreting District of Columbia law); *Dobre*, 850 F. Supp. at 288 (E.D. Pa.) (interpreting Pennsylvania law); *Conway v. City of Hartford*, 1997 WL 78585, at *6–7 (Conn. Super. Ct. Feb. 4, 1997); *Sommers v. Iowa Civil Rights Comm’n*, 337 N.W.2d 470, 474 (Iowa 1983).

105. *Lie*, 2002 WL 31492397, at *3–5; *Enriquez v. W. Jersey Health Sys.*, 777 A.2d 365, 371–73 (N.J. Super. Ct. App. Div. 2001).

106. *Maffei v. Kolaeton Indus., Inc.*, 626 N.Y.S.2d 391, 394–96 (N.Y. Sup. Ct. 1995).

107. 42 U.S.C. § 12211(b)(1) (2000) (ADA); 29 U.S.C. § 705(2)(F)(I) (Rehabilitation Act).

laws.¹⁰⁸ Both states define a “disability” or “handicap” as, roughly, a physical or mental impairment that substantially limits a major life activity.¹⁰⁹ And courts in both states have held that (1) transsexualism is not a physical impairment and (2) even if it is a mental impairment, it does not substantially limit any major life activity; therefore, it is not protected under the state’s law.¹¹⁰ As the Iowa Supreme Court put it, “[a] person who is anatomically of one sex but psychologically and emotionally of the other sex obviously has a grave problem, but that problem does not necessarily constitute the kind of mental condition that the legislature intended be treated as a substantial handicap to employment.”¹¹¹

On the other hand, courts in several states have recognized transsexualism as a handicap protected by state law. These states are divided into two categories. In the first category are states that, like Iowa and Pennsylvania, require plaintiffs to show substantial limitation of a major life activity, but whose courts construe that phrase more broadly than do Iowa and Pennsylvania courts. For instance, a Massachusetts trial court held that gender identity disorder qualifies as a handicap because it “often interferes with ordinary activities,” including “functioning at school or work”; moreover, “the need for ongoing medical care in the form of psychotherapy and hormone treatments may qualify as a substantial limitation on its own.”¹¹² Similarly, a trial court in New Hampshire ruled that transsexualism is a mental handicap because it substantially limits major life activities such as “social and occupational functioning” and “caring for oneself.”¹¹³

The second category of states accepting transsexualism as a disability or handicap consists of states that do not require a showing of substantial limitation of major life activities, but instead protect any condition that is medically accepted or diagnosable by accepted medical techniques. In these states, which include Connecticut, New Jersey,

108. *Dobre*, 850 F. Supp. at 288–90 (interpreting Pennsylvania law); *Sommers*, 337 N.W.2d at 474–77; see also *Holt v. N.W. Pa. Training P’ship Consortium, Inc.*, 694 A.2d 1134, 1139 (Pa. Commw. Ct. 1997) (agreeing with *Dobre*’s interpretation of Pennsylvania law).

109. *Dobre*, 850 F. Supp. at 288 (citing 16 Pa. CODE § 44.4 (1992)); *Sommers*, 337 N.W.2d at 474–75 (citing IOWA ADMIN. CODE r. 240-6.1(1)-(5) (1982)).

110. *Dobre*, 850 F. Supp. at 289; *Sommers*, 33 N.W.2d at 476–77.

111. *Sommers*, 33 N.W.2d at 476. The Supreme Court of Washington also has rejected a transsexual disability-discrimination claim, but it did so only because there was no evidence of discrimination in that particular case; unlike Iowa and Pennsylvania courts, it did not hold that transsexualism can never be a disability. See *Doe v. Boeing Co.*, 846 P.2d 531, 534–36 (Wash. 1993).

112. *Lie*, 2002 WL 31492397, at *5–6.

113. *Doe v. Electro-Craft Corp.*, 1988 WL 1091932, at *5 (N.H. Super. Ct. Apr. 8, 1988).

and New York, GID's status as a recognized mental disorder¹¹⁴ is sufficient to make transsexuals a protected class.¹¹⁵

One final note: there is another theory of disability discrimination that could be viable for transsexuals but has rarely been litigated. Some state laws protect not only employees who *have* a disability, but also employees who are *regarded as having* a disability by their employer. Accordingly, even if a state court rejects the idea that transsexualism is a disability, it still might be willing to afford relief to a transsexual plaintiff if the employer treated transsexualism like a disability. Only two courts have considered this argument; one (in Massachusetts) accepted it,¹¹⁶ and the other (in Pennsylvania) rejected it.¹¹⁷ While there is little case law on either side of this question, it provides yet another theory that is conceivably viable for transsexual plaintiffs.¹¹⁸

VI. Other Theories for Protecting Transsexuals from Discrimination

As recounted above, the major battles over transsexual employment rights are being fought under federal and state sex-discrimination laws, as well as state disability-discrimination laws. However, two other, miscellaneous theories occasionally pop up: transsexual discrimination characterized as (1) sexual-orientation discrimination and (2) "appearance discrimination."

Sexual orientation is not a protected class under federal law,¹¹⁹ but a growing number of states are adding it to their lists. In several of these states, transsexual plaintiffs have attempted to frame their claims as sexual-orientation discrimination, but they have met with unanimous failure: every state court to consider the question has held that transsexualism is distinguishable from sexual orientation and thus not protected under such laws.¹²⁰ As one court put it, transsexualism "is best understood as an issue of gender identity unrelated to sexual orientation. A psychiatric diagnosis of gender identity disorder is inde-

114. See DSM-IV, *supra* note 6, at 576.

115. *Conway*, 1997 WL 78585, at *4–5; *Enriquez*, 777 A.2d at 373–76; *Doe v. Bell*, 754 N.Y.S.2d 846, 850–51 (N.Y. Sup. Ct. 2003).

116. *Lie*, 2002 WL 31492397, at *7.

117. *Dobre*, 850 F. Supp. at 289–90.

118. Theoretically, this "regarded as" claim could be viable under federal law as well. See 42 U.S.C. § 12102(C). However, the only federal court to consider the theory rejected it. *Kastl*, 2004 WL 2008954, at *4 n.9.

119. *E.g.*, *Simonton v. Runyon*, 232 F.3d 33, 35 (2d Cir. 2000) ("The law is well-settled in this circuit and in all others to have reached the question that . . . Title VII does not prohibit harassment or discrimination because of sexual orientation.").

120. *Underwood*, 857 F. Supp. at 97–98 (interpreting District of Columbia law); *Conway*, 1997 WL 78585, at *7 n.2; *Lie*, 2002 WL 31492397, at *7–8; *Enriquez*, 777 A.2d at 370–71; *Maffei*, 626 N.Y.S.2d at 393.

Ironically, the *legislatures* of three other states (Illinois, Maine, and Minnesota) have expressly *included* transsexualism or gender identity in their definitions of sexual orientation. See Part II, *supra*.

pendent of an individual having a heterosexual, bisexual, or homosexual orientation.”¹²¹

However, one of the courts rejecting sexual-orientation claims by a transsexual left the door open for a related claim. This court, sitting in Massachusetts, noted that its state law also protects employees who suffer discrimination based on their *perceived* sexual orientation; accordingly, the court speculated that a transsexual might have a viable claim if, for example, an employer perceived the transsexual as a homosexual and discriminated on that basis.¹²² But there are no reported cases of transsexual plaintiffs successfully using this theory.

Finally, in one court, a transsexual survived a motion to dismiss by proffering the unique theory of appearance discrimination. District of Columbia law prohibits discrimination based on, *inter alia*, “personal appearance,” and one plaintiff successfully stated a claim under this provision by stating in her complaint that she was discharged “because she is a transsexual and retains some masculine traits.”¹²³

VII. Summary and Conclusion

Recall the original question posed: are transsexuals protected from employment discrimination? Or, to return to our original hypothetical, does Ron/Rhonda represent a lawsuit waiting to happen? As the body of this article confirms, the answer is: “it depends.” To find the precise answer, one must consider the following questions:

- A. Did the discrimination occur in a state (or locality) whose laws expressly protect transsexuals from discrimination?
- B. Did the discrimination occur in a federal jurisdiction that interprets Title VII and *Price Waterhouse* so as to protect transsexuals from sex discrimination?
- C. Did the discrimination occur in a state that has interpreted its own sex-discrimination laws so as to protect transsexuals?
- D. Did the discrimination occur in a state that considers transsexualism a disability or handicap protected from discrimination? If not, could the discrimination still be actionable because the employer regarded transsexualism as a disability or handicap?
- E. Did the discrimination occur in a state that forbids discrimination based on real or perceived sexual orientation? If so, could a court be persuaded that one’s gender identity is part of one’s sexual orientation or that the employer perceived the transsexual as a homosexual?
- F. Did the discrimination occur in a state (or locality) that forbids discrimination on the basis of “personal appearance” or the like?

121. *Lie*, 2002 WL 31492397, at *8.

122. *Id.*

123. *Underwood*, 857 F. Supp. at 97–99.

Only by considering each of these possibilities can one ascertain whether any particular transsexual enjoys protection from employment discrimination. And, of course, many jurisdictions have not decided these questions one way or another, adding an element of speculation to what is already a complex inquiry.

The legal status of transsexuals in the workplace is complicated and often uncertain. This is perhaps unsurprising; as one commentator put it, “[w]hile the law draws lines, a transsexual crosses lines.”¹²⁴ But as the protections for transsexuals continue to multiply, increased litigation is sure to follow, making it incumbent upon litigators, judges, and others who deal with employment law to understand the complex questions involved. Sooner or later, Ron/Rhonda is likely to show up in your office—or your client’s.

124. Debra Sherman Tedeschi, *The Predicament of the Transsexual Prisoner*, 5 TEMP. POL. & CIV. RTS. L. REV. 27, 27 (1995).

The Significance of the Sarbanes-Oxley Whistleblower Provisions

Daniel P. Westman*

I. Introduction

Three years of litigation under the whistleblower provisions of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) have illustrated how different litigation of such disputes can be from litigation of other types of employment disputes. This article discusses the Sarbanes-Oxley whistleblower provisions in the context of other preexisting whistleblower protection laws, how unique features of Sarbanes-Oxley have led to results that would be unusual in other types of employment litigation, how the Sarbanes-Oxley whistleblower provisions are affecting the development of state law, and how those provisions are influencing corporate governance practices.

II. How Sarbanes-Oxley Differs from Prior Whistleblower Protection Laws

A. *Broadened Scope of Subjects of Protected Disclosures*

The whistleblower provisions of Sarbanes-Oxley differ substantially from previous federal and state whistleblower protection laws. Until Sarbanes-Oxley, most federal and state whistleblower laws applicable to the private sector protected only employees who raised concerns about dangers to the public health or safety.¹ Most such laws did not protect private sector employees who raised concerns about fraud against shareholders, because such issues were not perceived as affecting public health or safety.

In contrast, most federal and state laws covering government sector whistleblowers did protect government employees who raised concerns about waste of funds.² The public interest in financial abuse in the government sector has always been clear because such abuse involves waste of taxpayer funds. However, until Sarbanes-Oxley, the issue of financial fraud in the private sector was viewed as of concern only to shareholders.

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1. See DANIEL P. WESTMAN & NANCY M. MODESITT, *WHISTLEBLOWING: THE LAW OF RETALIATORY DISCHARGE*, Ch. 4 and App. B (2d ed., BNA Books 2004) [hereinafter *WHISTLEBLOWING*].

2. *Id.*, at Ch. 3 and App. A.

Sarbanes-Oxley breaks through the conceptual barrier that previously caused public policy to be more narrowly defined in the private sector than the government sector. With the failures of several major corporations, and the corresponding investment losses suffered by millions of employees and shareholders, Congress decreed in Sarbanes-Oxley that fraud against shareholders is an issue of public concern justifying significant new civil and criminal protections for private sector employees who raise concerns about financial fraud. For the first time, Sarbanes-Oxley creates a civil remedy for whistleblowers in the private sector who raise concerns about financial matters that implicate violations of federal securities laws.³ Thus, the subject matter of protected disclosures has been significantly broadened beyond the categories of dangers to the public health and safety.

B. *“Undersight” as an Element of Securities Regulation*

Sarbanes-Oxley also uses whistleblower protection as a key component of federal securities law enforcement. The concept of “oversight” has been familiar to lawyers since the passage of the Securities Exchange Act of 1934, which created the Securities and Exchange Commission (SEC) to police the securities markets. “Gatekeepers,” such as public accounting firms and law firms, also have been viewed as having a role in overseeing the reporting of corporate financial data to ensure its accuracy. Of course, corporate boards of directors have been responsible for overseeing the operations of their corporations, including ensuring the accuracy of financial reports.

Oversight, however, did not prevent the frauds of recent years at companies such as Enron, WorldCom, Adelphia, and others. These events have shown how difficult it can be for corporate outsiders like the SEC, and accounting and law firms, to peer into the inner workings of corporations to determine whether financial fraud is occurring. Outsiders must rely on others to supply information about corporate financial reports, and that information may be misleading. Sarbanes-Oxley ensures that individuals at the operational level who are intimately

3. Section 806 of Sarbanes-Oxley creates a federal civil right of action on behalf of any employee of a publicly traded company, or any employee of a contractor of a publicly traded company, who is subject to discrimination in retaliation for reporting corporate fraud or accounting abuses. Sarbanes-Oxley Act, 18 U.S.C. § 1514(A) (2002). Section 806 prohibits publicly traded companies from discriminating against an employee in retaliation for any lawful act done by the employee to: (1) provide information or otherwise assist in any investigation regarding conduct that the employee reasonably believes constitutes a violation of federal securities fraud statutes or SEC rules, provided the investigation is conducted by a federal regulatory or law enforcement agency, any Member of Congress or congressional committee, or a person with managerial authority within the publicly traded corporation; or (2) file, testify, participate in, or otherwise assist in any proceeding related to an alleged violation of corporate fraud laws or regulations. *Id.*

involved in a company's business have the ability to inform outsiders when they see financial fraud.

"Undersight" is a term I have introduced to describe the concept of internal monitoring from the bottom up.⁴ Now, corporate insiders who observe the daily operations of companies are protected by Sarbanes-Oxley if they report concerns about financial fraud. In addition to strengthening "oversight" by creating the Public Company Accounting Oversight Board and mandating other actions, Sarbanes-Oxley also added new "undersight" provisions to protect corporate insiders who witness fraud firsthand.

Woven throughout Sarbanes-Oxley is the theme that protection of employees who report financial abuse may help to prevent future corporate collapses and securities frauds. The Report of the Senate Judiciary Committee on the bill that became Sarbanes-Oxley states: "In a variety of instances when corporate employees at both Enron and Andersen [the accounting firm which audited Enron's books] attempted to report or 'blow the whistle' on fraud, but (sic) they were discouraged at nearly every turn."⁵ Protection for employees engaging in "undersight" is reflected in many facets of Sarbanes-Oxley:

- Section 301 requires corporate Audit Committees to create mechanisms for receiving anonymous employee concerns about financial improprieties;⁶
- Section 806 creates new civil protection for employees who report concerns about alleged fraud upon shareholders,⁷ and section 1107 creates new criminal penalties for retaliation that extend more broadly than does section 806;⁸
- Section 307 requires the SEC to issue regulations setting forth minimum standards of practice applicable to attorneys who practice before the SEC.⁹ The rules issued by the SEC require attorneys who are aware of financial fraud by their clients to alert the issuers' executive management, and then the issuers' boards of directors if executive management does not respond appropriately;¹⁰
- Section 501 requires the SEC to promulgate rules that prohibit brokerage firms from retaliating against securities analysts because of an "unfavorable research report that may adversely affect the present or prospective investment banking relationship of the broker or dealer with the issuer that is the subject of the

4. WHISTLEBLOWING, *supra* note 1, at Ch. 1.III, 18–22.

5. S. REP. NO. 107–146, at 4–5 (2002).

6. 15 U.S.C. § 78fm(4) (2002).

7. 18 U.S.C. § 1514A (2002).

8. 18 U.S.C. § 1513 (2002).

9. *See* 17 C.F.R. pt. 205 (2005).

10. *Id.*

research report.”¹¹ This new legal protection for securities analysts was driven by concerns that brokerage firms were pressuring securities analysts to write overly favorable evaluations of stocks in order to obtain additional investment banking business; and

- Section 406 requires issuers of publicly traded securities to disclose whether they have codes of ethics applicable to senior financial officers.¹² Both the New York Stock Exchange and the National Association of Stock Dealers have gone further by requiring companies who wish to maintain their listings on those exchanges to implement Codes of Ethics not limited to executive management, and to include in such codes provisions that protect from retaliation employees who report alleged violations.¹³

Given Sarbanes-Oxley’s pervasive concern for whistleblower protection, it is not surprising that the statute contains substantive and procedural elements that are favorable to employees.

C. *Stronger Civil and Criminal Remedies for Reprisals*

Sarbanes-Oxley significantly strengthens the penalties for retaliation against whistleblowing. The civil provisions of Sarbanes-Oxley allow for immediate reinstatement of whistleblowing employees, even before an evidentiary hearing on the merits. The criminal provisions of Sarbanes-Oxley create severe penalties (including substantial fines and up to ten years in prison) for retaliation against whistleblowers who raise concerns about violation of *any* federal criminal statute, not simply laws limited to financial fraud.¹⁴ These criminal penalties may apply to *any* employer, regardless of whether the employer is publicly traded or privately held, and may apply to individual managers as well as to corporate employers.

1. Reinstatement

Reinstatement of employment has been required in Sarbanes-Oxley whistleblower cases in circumstances where such relief would be unlikely in other types of employment litigation. The statute and implementing regulations allow reinstatement of employment after investigations by OSHA investigators (to whom investigations have been delegated), but before any hearing on the merits before an administrative law judge (ALJ) with the U.S. Department of Labor (DOL).¹⁵ Re-

11. 15 U.S.C. § 780-6(a)(1)(c) (2002).

12. 15 U.S.C. § 7264(a) (2002).

13. See New York Stock Exchange Listed Company Manual, Section 303A; National Association of Securities Dealers, Inc., Rule 4350(m) and Interpretive Memorandum IM-4350-7.

14. 18 U.S.C. § 1513(e) (2002).

15. 18 U.S.C. § 1514A(b)(2)(A) (2002). See also 29 C.F.R. § 1980.105(a)(1) (2005).

instatement is not stayed even if the defendant requests a *de novo* hearing on the merits.¹⁶

This provision is not surprising in the DOL context because the DOL enforces whistleblower statutes in the nuclear energy, aviation, and other safety-sensitive industries. Because employees are viewed by the DOL as the front line of safety inspection inside the containment vessels of nuclear energy installations, or inside airport hangars, the DOL's view has been that reinstating a whistleblower to a position from which additional safety problems might be reported is the best way to deter unsafe conditions. From this perspective, immediately reinstating a Sarbanes-Oxley whistleblower theoretically aids in deterring potential financial fraud.

However, reinstatement in other types of employment litigation is an unusual remedy where the relationship between the parties has become adversarial. Therefore, it was a surprise to the employers in two cases when the ALJs ordered reinstatement of the employees. In *Welch v. Cardinal Bankshares Corp.*, the employer was a small bank that presented evidence to the ALJ that the bank's management, board of directors and shareholders all did not wish the plaintiff, who was the former chief financial officer, to return to his job.¹⁷ The ALJ reinstated the employee notwithstanding those objections.¹⁸ The bank has publicly stated it intends to appeal.¹⁹ In *Bechtel v. Competitive Technologies, Inc.*, the ALJ ordered reinstatement of two vice presidents who alleged that they had been terminated for raising concerns about financial fraud.²⁰ The employer objected strongly to the ALJ's order and delayed their reinstatement.²¹ The employees then sought and obtained an injunction in federal court compelling the employer to obey the ALJ's reinstatement order.²²

2. Criminal Penalties

Section 1107, titled "Retaliation Against Informants," imposes criminal penalties on any individual who "knowingly, with the intent to retaliate, takes any action harmful to any person, including interference with the lawful employment or livelihood of any person, for providing to a law enforcement officer any truthful information relating to the commission or possible commission of any Federal offense . . ."²³ This provision supplements the existing federal criminal penalties for

16. *Id.*

17. *Welch v. Cardinal Bankshares Corp.*, 2003-SOX-15, at 2, 10 (ALJ Feb. 15, 2005). A comprehensive library of whistleblower decisions is posted by the U.S. Department of Labor at <http://www.oalj.dol.gov/public/wblower/refrnc/sox1list.htm>.

18. *Id.* at 15.

19. *The Long, Lonely Battle of David E. Welch*, 115:8 U.S. BANKER (August 2005).

20. *Bechtel v. Competitive Tech, Inc.*, 2005-SOX-33, at 1-2, 8 (ALJ Mar. 29, 2005).

21. *Bechtel v. Competitive Tech., Inc.*, 369 F. Supp. 2d 233, 235 (D. Conn. 2005).

22. *Id.* at 237.

23. 18 U.S.C. § 1513(e) (2002).

witness intimidation. The penalties include a fine and/or imprisonment up to ten years.²⁴

In contrast to the civil remedies created by section 806, the criminal provisions of section 1107 are not limited to the actions of publicly traded companies, nor are they restricted in scope to matters involving corporate fraud or accounting abuses.²⁵ However, section 1107 is limited to “external” whistleblowers and does not, by its terms, protect “internal” whistleblowers who only voice concerns within their employers’ organizations.²⁶

The potential scope of this new criminal statute is very broad. Federal crimes have been created by many labor and employment statutes, including the Occupational Safety and Health Act (for making false statements, for giving advance notice of inspections),²⁷ the National Labor Relations Act (for loans by management to unions, for willfully interfering with agents of the Board, for employing as union employees felons convicted of certain crimes),²⁸ the Employee Retirement Income Security Act (for employing convicted felons as fiduciaries),²⁹ the Railway Labor Act (for refusal to obey certain sections of the statute),³⁰ and many more too numerous to list here. There are federal crimes in the environmental protection statutes, securities statutes, and the Food and Drug Act. In addition, corporations have been criminally prosecuted under the federal conspiracy statute, the Racketeer Influenced and Corrupt Organizations Act, the mail and wire fraud statutes, the Foreign Corrupt Practices Act, the tax laws, perjury statutes, and obstruction of justice statutes.

In reviewing these partial lists, it is apparent that many employees who provide information to law enforcement officials could potentially fall within the protections of the criminal provisions of Sarbanes-Oxley, and that many companies and individual managers could face criminal prosecutions under Sarbanes-Oxley.

3. Individual Liability

The civil provisions of section 806 apply broadly to prohibit retaliation by officers, employees, or agents of publicly traded companies.³¹ In contrast, many employment statutes prohibit only “employers” from engaging in retaliation, and such statutes have been construed not to

24. *Id.*

25. *Id.*

26. *Id.*

27. *See* 29 U.S.C. § 666 (2002).

28. *See* 29 U.S.C. §§ 186, 504 (2002).

29. *See* 29 U.S.C. § 1111 (2002).

30. *See* 45 U.S.C. § 152 (2002).

31. 18 U.S.C. § 1514A (2002).

provide remedies against individual managers.³² The regulations implementing Section 806 provide for individual liability.³³

The criminal provisions contained in section 1107 are phrased broadly as well, stating that “[w]hoever” interferes with the lawful employment of any person is guilty of a felony.³⁴ The author is not aware of any criminal prosecutions brought under section 1107. However, the availability of civil and criminal penalties against individuals demonstrates how aggressively Sarbanes-Oxley intends to deter retaliation against whistleblowers.

D. *Burdens of Proof Favorable to Employees*

The Sarbanes-Oxley whistleblower provisions set forth different burdens of proof for plaintiffs and defendants. In most civil litigation, both the plaintiff and defendant must prove their cases by a “preponderance” of the evidence, meaning that the judge or jury finds that the evidence of one party is more likely to be true than the evidence of the other party.

Under the Sarbanes-Oxley whistleblower provisions, however, the relatively light “preponderance” of the evidence burden is applicable only to plaintiffs.³⁵ In contrast, defendants must prove that they did not retaliate against plaintiffs by “clear and convincing” evidence, usually meaning evidence producing “a firm belief or conviction.”³⁶ This is a heavier burden than the “preponderance” standard, though not as difficult to satisfy as the “beyond a reasonable doubt” standard used in criminal cases.

Several decisions under the Sarbanes-Oxley whistleblower provisions have reached results in favor of employees that appear to have been driven by these differing burdens of proof. For example, in *Platone v. Atl. Coast Airlines* and *Welch v. Cardinal Bankshares Corp.*, the employees were found to have met their burdens of proving by a preponderance of the evidence that they had a reasonable, good-faith belief that they had raised concerns about financial fraud, but the defendants were found not to have satisfied the “clear and convincing” standard.³⁷

In both cases, the defendants argued that they had good reasons to terminate the plaintiffs. In *Platone*, the plaintiff’s job was to represent management’s position in dealings with the company’s labor

32. See, e.g., *Reno v. Baird*, 957 P.2d 1333 (Cal. 1998) (interpreting antidiscrimination provisions of California Fair Employment and Housing Act).

33. 29 C.F.R. § 1980.101 (2005).

34. 18 U.S.C. § 1513(e) (2002).

35. *Stone & Webster Eng’g Corp. v. Herman*, 115 F.3d 1568, 1572 (11th Cir. 1997).

36. *Id.*

37. *Platone v. Atl. Coast Airlines*, 2003-SOX-27, at 28 (ALJ Apr. 30, 2004); *Welch v. Cardinal Bankshores Corp.*, 2003-SOX-15, at 47 (ALJ Jan. 28, 2004).

unions.³⁸ The defendant argued that Ms. Platone was terminated because she had concealed from the defendant that she was having a romantic relationship with the representative of one of the company's unions.³⁹ Perhaps the defendant would have persuaded the ALJ that concealing a potentially compromising relationship was the real reason for the plaintiff's discharge under the preponderance of the evidence standard. However, the ALJ ruled that the defendant had not proven by clear and convincing evidence that the romantic relationship was the true reason for the termination.⁴⁰

In *Welch*, the plaintiff was the chief financial officer of a small bank who raised concerns about potential financial fraud.⁴¹ The bank terminated his employment when the plaintiff refused to talk with the bank about his concerns unless his attorney was present.⁴² The ALJ ruled that the plaintiff had proven by a preponderance of the evidence that he had a good faith belief in his report, but that the defendant bank had not proven its defense of failure to cooperate in the bank's investigation by clear and convincing evidence.⁴³

E. *The Diminished Role of "Materiality"*

Under the civil remedy created by section 806, employees need only "reasonably believe" that they are reporting a violation of securities fraud statutes or SEC rules.⁴⁴ As discussed above, employees need only prove their reasonable belief by a preponderance of the evidence. Under the criminal provisions of section 1107, employees are protected for reporting "truthful information," whether or not the information proves a violation of law.⁴⁵

The "reasonable belief" standard under section 806 has generated anomalous results to date in several cases in which the employer defended the case on the ground that the alleged fraud complained about by employees did not satisfy the "materiality" standard under federal securities law. In one case, the plaintiff worked in the accounts payable department and alleged that he had been instructed to delay payments of invoices until later quarters of the fiscal year.⁴⁶ The employer used the accrual method of accounting, which meant that the invoices were reflected on the company's books at the time the invoices were received, not when they were paid.⁴⁷ Accordingly, the company argued that it was legally impossible for there to have been any securities fraud, be-

38. *Platone*, 2003-SOX-27, at 5.

39. *Id.* at 28.

40. *Id.*

41. *Welch*, 2003-SOX-15, at 3, 15 (ALJ Jan. 28, 2004).

42. *Id.* at 34.

43. *Id.* at 47.

44. 18 U.S.C. § 1514A(a)(1) (2002).

45. 18 U.S.C. § 1513(e) (2002).

46. *Halloum v. Intel Corp.*, 2003-SOX-7, at 1 (ALJ Mar. 4, 2004).

47. *Id.* at 2.

cause delaying the payments of the invoices until later quarters could not have had any effect on the financial statements of the company.⁴⁸ Nevertheless, the ALJ found that the employee had satisfied his burden of proving that he had a “reasonable belief” that a violation of statute or regulation had occurred.⁴⁹

The regulations promulgated under Sarbanes-Oxley allow the SEC to weigh in on securities issues by participating in proceedings under section 806 as *amicus curiae*.⁵⁰ However, to date the SEC does not appear to have acted as *amicus curiae* in any significant way. The parties in Sarbanes-Oxley whistleblower litigation should assume that they, and not the SEC, will have to explain how federal securities law plays into each case.

F. *Enhanced Credibility of Anonymous Complaints*

Prior to Sarbanes-Oxley, anonymous employee complaints often were hard to take seriously. Anonymous complaints could be difficult to investigate if the complaints did not provide sufficient details, and it could be difficult or impossible to ask follow-up questions of an anonymous source. Also, the unwillingness of anonymous complainants to identify themselves may have undermined their credibility in some eyes.

Section 301 of Sarbanes-Oxley requires audit committees of publicly traded companies to implement mechanisms for receipt, investigation, and tracking of anonymous employee complaints.⁵¹ Now, employees know that anonymous complaints cannot be summarily dismissed by management but must be taken seriously by a committee of the board of directors.

G. *Potential for Claims by Lawyers, Accountants, and Other “Gatekeepers”*

Sarbanes-Oxley does not apply solely to publicly traded companies. The criminal protections set forth in section 1107 are not limited to publicly traded companies. The civil whistleblower protections in section 806 apply on their face to “contractors” of publicly traded companies.⁵² This is easily remembered if one recalls the example discussed in the congressional debates of employees of the Arthur Andersen accounting firm who could not effectively blow the whistle on fraud at Enron. Congress apparently wished to protect employees of accounting firms, law firms, or other contractors who report concerns about financial fraud, whether the contractors themselves are privately or publicly

48. *Id.* at 13.

49. *Id.* at 10.

50. See 29 C.F.R. §§ 1980.104(a) (copies of complaints are provided to the SEC), §§ 1980.108(b) (SEC may act as *amicus curiae*).

51. 15 U.S.C. § 78f(m)(4) (2002).

52. 18 U.S.C. § 1514A(a) (2002).

held. Also, the early cases decided under Sarbanes-Oxley have protected employees of privately held subsidiaries of publicly traded companies on the theory that the finances of the private subsidiaries have an effect on the financial reports of the public parents.⁵³

Applying these principles in practice, it is clear that many privately held enterprises, including investment banks, accounting firms, and law firms, may be subject to both the civil and criminal whistleblower provisions of Sarbanes-Oxley.

H. *The Attorney Whistleblower Rules*

Sarbanes-Oxley requires the SEC to promulgate rules of professional responsibility that require attorneys to report material violations of federal securities law to their clients' chief legal counsel or chief executive, or, if such officers do not respond appropriately, to their clients' boards of directors.⁵⁴ The SEC has promulgated rules that broadly define which attorneys are viewed as practicing before the SEC, which include attorneys who work both in corporate legal departments and in outside law firms.⁵⁵

These provisions create the possibility for Sarbanes-Oxley whistleblower claims by attorneys who allege that their employment was terminated in retaliation for carrying out their legal obligations under the SEC rules. To be sure, the ethical obligation of attorneys to preserve attorney-client confidences may present an obstacle to such actions. The Administrative Review Board (ARB) within the DOL has ruled as a matter of federal common law that whistleblowers may not use attorney-client privileged information offensively in order to prove their cases but may use privileged information only to defend themselves.⁵⁶ While the author is not aware of any Sarbanes-Oxley claims having been filed by attorneys as of this date, prudent companies and law firms should anticipate such claims and implement practices to minimize their risks.

III. The Effect of Sarbanes-Oxley's Whistleblower Provisions on State Law

Federal laws of the magnitude of Sarbanes-Oxley often significantly affect the development of state law. At least two state legislatures, those of California⁵⁷ and Connecticut,⁵⁸ have enacted whistleblower protection statutes paralleling the civil provisions contained in section 806 of Sarbanes-Oxley. Equally if not more significant may be the effect of Sarbanes-Oxley on the development of the common law.

53. See *Morefield v. Exelon Serv., Inc.*, 2004-SOX-2, at 2 (ALJ Jan. 28, 2004).

54. 15 U.S.C. § 7245 (2002).

55. 17 C.F.R. pt. 205.

56. See *Willy v. The Coastal Corp.*, ARB No. 98-060, at 23 (ARB Feb. 27, 2004).

57. See CAL. LAB. CODE § 1102.5 (Deering 2005).

58. 2003 Conn. Acts 03-259 (Reg Sess.).

A. *Wrongful Termination in Violation of Public Policy*

The Sarbanes-Oxley whistleblower provisions may have a significant effect upon the development of the common law theory of wrongful termination in violation of public policy. Many states allow such causes of action to be premised upon federal statutes.⁵⁹ Even before Sarbanes-Oxley, one court began its opinion in a case allowing the plaintiff to proceed with a claim for wrongful termination in violation of public policy as follows: “With the sole exception of the war on terrorism, no issue dominates current thought more than the corporate and accounting ethical scandals which have rocked our country.”⁶⁰ In the aftermath of Sarbanes-Oxley, it is conceivable that some state courts may recognize claims for wrongful termination in violation of public policy predicated on either the civil provisions of section 806 or the criminal provisions of section 1107.

B. *Breach of Implied Contract*

Similarly, state courts may recognize causes of action for breach of implied contract based upon codes of ethics required by the national stock exchanges. Under section 405 of Sarbanes-Oxley, publicly traded companies are required to disclose whether they have codes of ethics applicable to senior executive officers.⁶¹ In response, the New York Stock Exchange and the National Association of Stock Dealers have issued rules that require companies listed on those exchanges to adopt codes of conduct or ethics applicable to all employees, not just senior executives, and requiring that such codes contain a provision forbidding retaliation against employees who disclose potential violations of the codes.⁶² As a result, most publicly traded companies now have codes of conduct or ethics that forbid retaliation against employees who raise concerns about violations of those codes.

In many states, written employment policies such as codes of conduct may be the basis for lawsuits for breach of contract.⁶³ Accordingly, some states may permit breach of contract claims by employees who allege that they were terminated in violation of the antiretaliation provision contained in a code of conduct or ethics. Some jurisdictions allow employers to avoid liability for breach of contract by use of prominent disclaimers stating that the policies do not create enforceable contractual rights.⁶⁴ However, use of disclaimers may undermine the effec-

59. See WHISTLEBLOWING, *supra* note 1, at Ch. 5.I.C., 99–100.

60. McGarrity v. Berlin Metals, Inc., 774 N.E.2d 71, 74 (Ind. Ct. App. 2002).

61. 15 U.S.C. § 7264(a) (2002).

62. See New York Stock Exchange Corporate Governance Rules, Section 303A of the NYSE Listed Company Manual; National Association of Stock Dealers, Inc., Rule 4350(m), and Interpretive Memorandum IM-4350-7.

63. WILLIAM J. HOLLOWAY & MICHAEL J. LEECH, EMPLOYMENT TERMINATION RIGHTS AND REMEDIES App. C (2d ed. 1993 & Supp. 2003).

64. *Id.*

tiveness of the codes by discouraging employees from making disclosures, which may cause the codes to be deemed insufficient under the stock exchange rules. Because many codes of conduct or ethics are broadly worded to encourage “honest and ethical” behavior, a very broad range of employee concerns may be protected beyond the subject of financial fraud against shareholders.

IV. Other Corporate Governance Effects

A. Privately Held Companies

While primarily aimed at reforming corporate governance of publicly traded companies, Sarbanes-Oxley has sparked discussion among privately held companies about whether Sarbanes-Oxley’s provisions should be adopted as “best practices,” including the whistleblower provisions. For example, charitable organizations that rely on donations for their existence have asked why their donors are any less entitled to corporate transparency than shareholders of publicly traded companies and why employees of charitable organizations should not be protected for raising concerns about misuse of donations.

B. Overseas Issues

In addition to spilling over from publicly traded to privately held entities, the Sarbanes-Oxley whistleblower protections may spread to countries outside the United States. At present, the only law on the issue appears to be that overseas employees of foreign subsidiaries of U.S. parent corporations are not protected by the Sarbanes-Oxley whistleblower provisions.⁶⁵ Nevertheless, U.S. parents intent on eliminating fraud overseas may wish to use codes of conduct or ethics to encourage foreign employees to report potential violations.

Requiring overseas employees to report violations may violate the privacy laws of other countries, or cultural sensitivities. Many countries have had repressive governments that encouraged informants to report on behavior of neighbors and co-workers. In some such countries, elaborate privacy laws have been enacted that forbid reporting illegal behavior of co-workers to anyone other than the proper governmental authorities. In other countries, individuals identify so strongly with groups to which they belong that it would be contrary to their culture for a whistleblower to bring shame upon the group by suggesting that someone in the group acted improperly. Thus, any employer thinking of implementing whistleblower policies outside the United States should carefully consider the legal and cultural climate of each specific country.

C. Additional Legal and Cultural Developments

“All that is necessary for the triumph of evil is that good men do nothing.” Edmund Burke’s famous eighteenth century dictum encaps-

65. *Carnero v. Boston Scientific Corp.*, No. 04-10031-RWZ, 2004 U.S. Dist. LEXIS 17205, at *5 (D. Mass. Aug. 27, 2004).

sulates why compliance efforts cannot rely on written policies or codes of conduct alone. After all, Enron had policies on paper forbidding the practices that brought down the company. Without people willing to report violations of law or codes of conduct, compliance efforts inevitably will be frustrated. The whistleblower provisions of Sarbanes-Oxley, coupled with growing acceptance of whistleblowing in both the law and popular culture, may create a climate in which employees more frequently engage in “undersight” to report violations of law, rather than doing nothing.

There is growing recognition in the law, apart from Sarbanes-Oxley, that protection against retaliation is an essential component of any statutory enforcement scheme. Recently, the U.S. Supreme Court held that protection against retaliation is necessary to enforcement of Title IX of the Education Amendments of 1972, even though Title IX itself did not contain a provision forbidding retaliation. In *Jackson v. Birmingham Board of Education*, a male coach of a girls’ high school basketball team alleged that his employment had been terminated in retaliation for his complaints that the girls’ team was underfunded in violation of Title IX.⁶⁶ Acknowledging that Title IX itself did not contain a provision forbidding retaliation, the Court implied a private right of action for retaliation.⁶⁷ The Court stated: “Reporting incidents of discrimination is integral to Title IX enforcement and would be discouraged if retaliation against those who report went unpunished. Indeed, if retaliation were not prohibited, Title IX’s enforcement scheme would unravel.”⁶⁸

Popular culture has kept pace with these legal developments. Today, whistleblowers may be held up to public esteem, as occurred in the December 30, 2002, issue of *TIME* magazine.⁶⁹ The cover of that issue named “The Whistleblowers” as Persons of the Year, and carried a photograph of Cynthia Cooper of WorldCom, Colleen Rowley of the FBI, and Sherron Watkins of Enron.⁷⁰ Hollywood has sympathetically portrayed whistleblowers in films including *Erin Brockovich* and *The Insider*.⁷¹

D. *Will Legal Protections for “Undersight” Create Cultures of Compliance?*

Fraud examiners have long known that the most common source of tips reporting fraud originate from employees. In 2004, the Association of Certified Fraud Examiners reported that over 40 percent of

66. *Jackson v. Birmingham Bd. of Educ.*, 125 S. Ct. 1497, 1500 (U.S. 2005).

67. *Id.* at 1507.

68. *Id.* at 1508.

69. *Persons of the Year*, *TIME* MAGAZINE, Dec. 30, 2002.

70. *Id.*

71. See *ERIN BROCKOVICH* (Universal Pictures 2000); *THE INSIDER* (Buena Vista Pictures Distribution 1999).

corporate fraud was discovered through employee tips.⁷² However, fear of being ostracized or fired may have deterred some employees from blowing the whistle in the past. After Sarbanes-Oxley, the question is whether the significant changes in legal protections for whistleblowers, coupled with more favorable depictions in the popular culture, will encourage employees to engage in “undersight” with greater frequency. A number of factors suggest that employees may more freely report legal or ethical violations today than in the past.

First, high ranking executives now have a compelling personal interest in knowing whether fraud is occurring within their organizations. Thanks to section 302 of Sarbanes-Oxley, CEOs and CFOs must personally certify the accuracy of corporate financial reports, on pain of criminal prosecution.⁷³ Employees who engage in “undersight” and disclose potential fraud may help to ferret out fraud, thereby improving the accuracy of financial reports and lessening the risk of prosecutions against CEOs and CFOs. Realizing this, executives may devote sufficient resources to compliance to convince the workforce to actively report potential fraud.

Second, Sarbanes-Oxley requires investigation of anonymous employee complaints. To the extent that fear of retaliation has deterred employees from identifying themselves by openly raising concerns, the ability to make anonymous complaints knowing that such complaints must be investigated may encourage whistleblowing.

Third, popular culture has long been ambivalent about “informing on” or “turning in” co-workers. Pejorative terms such as “fink” or “stool pigeon” exemplify such ambivalence. However, almost every American who had an investment in the stock markets suffered significantly by the meltdowns of Enron, WorldCom, and others, and the resulting stock market collapse. Today, employees may feel that reporting potential fraud is necessary to protect their own personal financial interests, as well as the interests of the investing public. After Sarbanes-Oxley, it may not be as easy to turn a blind eye to fraud based on the rationalization that “it’s not my problem.”

E. *Steps Employers May Take to Avoid Whistleblower Litigation*

A whistleblower claim can generate negative publicity that may undermine investor confidence, draw the attention of regulators, and weaken employee morale and loyalty. Some basic steps can help to avoid such claims.⁷⁴

72. Association of Certified Fraud Examiners, *2004 Report to the Nation on Occupational Fraud and Abuse*, at 20.

73. 15 U.S.C. § 7241 (2002).

74. See generally WHISTLEBLOWING, *supra* note 1, at Ch. 10, 263–78.

1. Establish an Employee Concerns Program

Establishing a forum in which employees can raise concerns and have some assurance that their concerns will be investigated can be an effective means of resolving an employee's grievance before a lawsuit is filed. In addition, an Employee Concerns Program can help alert management to wrongdoing early on, providing an opportunity to intervene and prevent further damage.

2. Train Managers and Supervisors to Instill a Corporate Culture of Compliance

One of the lessons of the recent accounting scandals is the importance of maintaining a culture conducive to raising concerns. Indeed, Congress appears to have concluded that many of the companies whose conduct precipitated Sarbanes-Oxley had cultures in which employees were dissuaded from asking probing questions. Managers and supervisors should be trained to encourage employees to raise concerns without fear of reprisal.

3. Take Disciplinary Action Against Those Who Engage in Retaliation

All employees should be put on notice (e.g., through training and the employee handbook) that if they retaliate, harass, or discriminate against another employee for raising a concern, they will be subject to disciplinary action.

4. Document Performance Issues, Contemporaneously

In defending against a whistleblower claim, to satisfy the "clear and convincing" burden, it is critical to have thorough, unambiguous evidence demonstrating that the same unfavorable personnel action would have been taken in the absence of the plaintiff's protected conduct. Accordingly, managers should thoroughly document performance issues on a routine basis. If there is not a contemporaneous documentary record of performance issues, then it may appear that the employer is making up performance issues after the fact to justify the adverse personnel action.

V. Conclusion

Sarbanes-Oxley clearly intends to deter future repetitions of Enron, WorldCom, and the like by encouraging employee whistleblowing about fraud on the financial markets. The U.S. capital markets have been the primary engine of the world's economic growth in the last several centuries. If the Sarbanes-Oxley whistleblower provisions that facilitate "undersight" actually work in practice to deter frauds, then they may be among the most significant employment law developments in recent times.

San Manuel Indian Bingo and Casino: Centrally Located in the Broad Perspective of Indian Law

Richard G. McCracken*

I. Thesis: As Indian Enterprises Like Casinos Grow and Enter Interstate Commerce in Ways Indistinguishable from Non-Indian Competitors, Federal Laws, Including Labor and Employment Laws, Will Be Asserted

In *San Manuel Indian Bingo & Casino*, the National Labor Relations Board decided that it had jurisdiction over business enterprises conducted on reservation lands by Native American tribes.¹ In this case, the business is a casino. The Board held that tribal sovereign immunity did not prevent its assertion of jurisdiction.² It reasoned that tribes are not either part of the federal government or States or their political subdivisions and therefore they are not covered by the governmental exemption from the National Labor Relations Act. Moreover, there is no express exclusion of tribes or their businesses from the coverage of the NLRA. The Board then turned to the question whether federal Indian policy precluded jurisdiction.³ Applying the line of analysis in *Donovan v. Coeur d'Alene Tribal Farm*, based on *Federal Power Comm. v. Tuscarora Indian Nation*, the Board determined that the NLRA is a statute of general application and presumptively applies to tribal enterprises unless it touches upon purely intramural matters such as tribal membership and inheritance or abrogates treaty rights, or there is legislative text or history showing a congressional intent to exclude these businesses.⁴ The Board found that none of these exceptions existed. The case was before the Board on the tribal employer's motion for summary judgment on jurisdictional grounds, which was denied. The case was remanded for hearing, but the employer then admitted the material factual allegations of the complaint and the general counsel moved for summary judgment. The Board has granted the

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1. *San Manuel Indian Bingo & Casino*, 341 N.L.R.B. 138, 174 L.R.R.M. (BNA) 1489 (2004), *overruling* *Fort Apache Timber Co.*, 226 N.L.R.B. 503 (1976).

2. *San Manuel*, 341 N.L.R.B. at 138, 174 L.R.R.M. (BNA) at 1489.

3. *Id.*, 341 N.L.R.B. at 138, 174 L.R.R.M. (BNA) at 1491.

4. *Id.*, 341 N.L.R.B. at 138, 174 L.R.R.M. (BNA) at 1492.

general counsel's motion and reaffirmed its decision about jurisdiction.⁵ It issued a cease-and-desist order.⁶ The employer has petitioned the District of Columbia Circuit Court of Appeals for review of the order.

A prominent lawyer representing Native American interests said that as tribal enterprises become larger and more involved with the larger, non-Indian world, there will be an ineluctable tendency for other governments to assert themselves. The *San Manuel* case is the latest proof that this view is correct.⁷ It is only the latest evidence, however, not the first or even most important. Over the past two decades, the federal courts have been moved steadily to regulate tribal enterprises in many ways, including employment. The Board in *San Manuel* just caught up with the dominant view of the federal courts that federal labor and employment laws apply to tribal enterprises on and off reservations.⁸

The federal courts' decisions have made it clear that Native American tribes are not going to be allowed to engage in businesses indistinguishable from those operated by non-Indians but free of any of the regulatory laws to which their non-Indian competitors are subject. Native American tribes would be wise to accept this and adapt their businesses to work within the federal regulatory framework. This outcome is inevitable and resisting it only wastes resources and creates disappointment and bitterness.

The outcome is inevitable because of fundamental principles. First, there is no doctrine of Indian sovereignty *vis-à-vis* the federal government. Such a doctrine has not existed and could not exist. The founding fathers held that *imperium in imperio* is a solecism in politics.⁹ When the Native American nations were conquered, it was inconceivable that they could be given sovereignty co-equal with that of the federal government. If the tribes were allowed to operate large-scale enterprises in interstate commerce subject only to tribal law, the situation would eventually become intolerable politically, for the supremacy of the federal government would be impaired.

Second, the essential tenet of free enterprise is that all competitors will struggle in the same regulatory environment so that it is their resources and ingenuity that provide the advantage. If the government gives one type of competitor a special regulatory advantage, competition is compromised. For that reason, as a general rule, nonprofit organizations are not allowed to engage in businesses unrelated to their nonprofit missions in competition with for-profit entities, without sub-

5. *Id.*, 341 N.L.R.B. at 138, 174 L.R.R.M. (BNA) at 1499.

6. *Id.*, 345 N.L.R.B. at 79.

7. *Id.*, 341 N.L.R.B. at 138, 174 L.R.R.M. (BNA) at 1489.

8. *Id.*

9. JACK RAKOVE, ORIGINAL MEANINGS: POLITICS AND IDEAS IN THE MAKING OF THE CONSTITUTION 182 (1997).

jecting themselves to the same tax burden as those entities. This prevents the obviously unfair advantage nonprofits would otherwise enjoy, for they would be able to expand more rapidly and cheaply for no other reason than government favor. The same is true of tribal enterprises. When they are extended beyond traditional, intramural activities, in competition with non-Indian businesses, they cannot long enjoy a vast competitive advantage conferred only by a differential government attitude toward them.

In this regard, the *San Manuel* case was most opportune. The San Manuel Casino is not a small business. It is not an "Indian" business in any other sense than its ownership by the San Manuel Band of Serrano Mission Indians. The vast majority of the casino's approximately 1,400 employees are made up of non-Indians who reside in California, off the Band's property. The casino is 6.2 miles from the City of San Bernardino and 60 miles from the City of Los Angeles. About 1.8 million people live within 25 miles of it. It conducts gambling operations patronized almost entirely by non-Indians. It includes a very large bingo hall, card games, and over 1,000 video gaming machines. It has 115,000 square feet, approximately 95,000 square feet of which is for gamblers.¹⁰ It also sells food and beverage to patrons. Unquestionably, it is in direct competition with non-Indian gaming, including racetracks and card clubs in California and casinos in Las Vegas. From an economic standpoint, what sense does it make for the non-Indian competitors to be subject to the full panoply of federal labor laws, and the San Manuel Casino subject to none? Even with the assertion of federal labor law, the non-Indian competitors are still at some disadvantage from government regulation, since they are subject to state labor and employment laws. Just as clearly as federal law can be applied to Native American businesses, state laws cannot be applied unless Congress makes them applicable.

Third, the central purpose of government is to protect its citizens. Very few Native Americans work in the casinos. Most of the workforce is non-Indian and comes from outside the reservation. Almost all the customers are non-Indian.¹¹ Those who hold to an extreme view of Indian sovereignty would leave the protection of workers and customers (and non-Indian businesses dealing with tribal enterprises) to the tribes exclusively. While I am not saying that federal government or state government is better than tribal government, I think it is clear that there is a natural tendency for government to assert itself when it feels the necessity to do so to protect its citizens. The workers, customers,

10. Because *San Manuel* was decided on a motion for summary judgment made on jurisdictional grounds and there has been no hearing, these facts are not in the decision but were presented to the Board by the charging party in declarations opposing the motion.

11. *San Manuel*, 341 N.L.R.B. at 140, 174 L.R.R.M. (BNA) at 1491.

and businesses dealing with tribal enterprises are citizens of the federal government, not of the tribe. They cannot participate in tribal government in any way. Because they are constituents of the federal government and not of the tribal government, it is only natural that the federal government will tend to exercise its right and ability to protect them. The *San Manuel* case was opportune in this regard, as well, because almost all of the employees of the casino are non-Indian.

Some might tend to regard the *San Manuel* decision as simple bureaucratic expansionism. This Board, however, has not shown a proclivity to expand its jurisdiction.¹²

Another favored way to explain new directions in Board policy is “politics,” in the sense of Republican versus Democratic or, as the party labels have come to signify in the NLRB world, favoring employer interests or union interests. That kind of thinking also does not explain the *San Manuel* decision. The majority included Chairman Battista, one of the Board’s Republicans, and was bipartisan.¹³ In September, there was a bill introduced in Congress by Representative Hayworth of Arizona to amend the MLRA to overturn the *San Manuel* decision.¹⁴ It was defeated by a bipartisan majority.¹⁵

Undoubtedly, this decision is viewed in Indian country as yet another example of the hostility of the non-Indian legal system to Native American interests. It is true that claims of Indian sovereignty have not been faring well in the courts. Whether this is because attempts have been made to expand the doctrine too far or because of hostility to Native Americans, or even racism, will remain a matter of opinion. Opinions about whether this kind of motivation exists are unlikely to alter the limited judicial acceptance of the notion of Indian sovereignty as a factor in interstate commerce.

II. General Law of Indian Sovereignty

Indian tribes have some attributes of sovereignty, but these are frequently misunderstood and overstated. Tribes are not akin to foreign nations with which the United States has “state-to-state” relationships. Indian tribes enjoy a limited sovereignty only by the grace of Congress.¹⁶ “The sovereignty that the Indian tribes retain is of a unique and limited character. It exists only at the sufferance of Congress and is subject to complete defeasance.”¹⁷

12. See, e.g., *Brown University*, 342 N.L.R.B., 175 L.R.R.M. (BNA) 1089 (2004), *overruling New York University*, 332 N.L.R.B. 1205 (2000).

13. *San Manuel*, 341 N.L.R.B. at 140, 174 L.R.R.M. (BNA) at 1491.

14. Tribal Relations Restoration Act of 2004, H.R. 4906, 108th Cong. (2004).

15. *Id.*

16. *United States v. Wheeler*, 435 U.S. 313, 323 (1978).

17. *Id.*

The Constitution does not give Indian tribes any sovereign rights.¹⁸ The Constitution, Art. I, § 8, cl. 3, gives the federal government plenary authority over Indian affairs.¹⁹ Therefore, congressional law is the source of whatever rights Indian tribes possess, and Congress may restrict or modify those rights as it chooses. For example, in *Escondido Mutual Water Co.*, an Indian tribe argued that a federal agency could not issue hydroelectric power licenses on reservation land without the tribe's consent.²⁰ The Court rejected this argument: "[I]t is clear that all aspects of Indian sovereignty are subject to defeasance by Congress . . . [and] Congress intended to [regulate the issuance of hydroelectric licenses on Indian lands] without the consent of the tribes involved."²¹

The tribes are therefore recognized to be not independent units of government. They are "dependents" of the United States.²² This is no recent development. Indian tribes have been described by the Supreme Court as "domestic dependent nations" since *Cherokee Nation v. Georgia*.²³

Such sovereign powers Indian tribes possess are limited to what is needed for self-government.²⁴ Tribes have criminal jurisdiction only over their own members.²⁵ Their criminal jurisdiction does not extend to nonmembers, even for offenses committed on reservation lands.²⁶ This was taken further in *Montana v. Blackfeet*, where the Court announced "the general proposition that the inherent sovereign powers of an Indian tribe do not extend to the activities of nonmembers of the tribe."²⁷ "Tribal assertion of *regulatory* authority over nonmembers must be connected to that right of the Indians to make their own laws and be governed by them."²⁸ There is a tendency to treat this standard expansively, for instance to contend that the proceeds from commercial endeavors in or outside Indian country are necessary for self-government because many of the valuable programs tribes adopt for

18. U.S. CONST. ART. I.

19. *Montana v. Blackfeet Tribe of Indians*, 471 U.S. 759, 764–65 (1985).

20. *Escondido Mut. Water Co. v. La Jolla Band of Mission Indians*, 466 U.S. 765, 787 n.30 (1984).

21. *Id.* This means that the federal government has the power to regulate or tax Indian enterprises, whether on or off the reservation. See *Superintendent of Five Civilized Tribes v. Comm'r of Internal Revenue*, 295 U.S. 418, 421 (1935) (income tax for on-reservation land); *Escondido Mut. Water Co.*, 466 U.S. at 787 n.30 (hydroelectric power license for reservation lands); *Wheeler*, 435 U.S. at 330–331 (unrestricted federal jurisdiction to define and punish crimes on reservation land, notwithstanding tribal court rulings on same charges).

22. *Duro v. Reina*, 495 U.S. 676, 686 (1990) ("dependent status"); *Oliphant v. Suquamish Indian Tribe*, 435 U.S. 191, 196 (1978) (quoting court of appeals) ("conquered and dependent").

23. *Cherokee Nation v. Georgia*, 30 U.S. 1, 17 (1831).

24. *Oliphant*, 435 U.S. at 196 n.6.

25. *Id.* at 195.

26. *Id.*

27. *Montana v. Blackfeet*, 450 U.S. 544, 565 (1981).

28. *Nevada v. Hicks*, 533 U.S. 353, 361 (2001) (emphasis added).

their members can only be financed this way.²⁹ The Supreme Court sees the principle much more narrowly, however. The laws tribes have the right to make and enforce are limited to purely intramural matters.

In *Strate v. A-1 Contractors*, 520 U.S. 438 (1997), we explained that what is necessary to protect tribal self-government and control internal relations can be understood by looking at the examples of tribal power to which Montana referred: tribes have authority “[to *punish tribal offenders*,] to determine tribal *membership*, to regulate *domestic relations* among members, and to prescribe rules of *inheritance* for members,” 520 U.S., at 459 (brackets in original), quoting Montana, *supra*, at 564. These examples show, we said, that Indians have “the right . . . to make their own laws and be ruled by them,” 520 U.S., at 459 (quoting *Williams v. Lee*, 358 U.S. 217, 220 (1959)).³⁰

Indian tribes, their members, and their enterprises are not immune from state law either, although the application of state law is much more limited than federal law. Once Indians go beyond reservation boundaries, they are generally held subject to nondiscriminatory state laws that otherwise apply to all citizens. In *Mescalero Apache Tribe*, the Supreme Court upheld New Mexico’s right to apply a gross receipts tax on a ski resort operated by an Indian tribe off its reservation, on land leased under the Indian Reorganization Act, 25 U.S.C. § 465.³¹ There is thus no question that both the states and the federal government may regulate and tax Indian activity off the reservation.³²

In *Nevada v. Hicks*, the Court made a very strong statement about the considerable power States have to regulate *on reservations* that should dispel many misimpressions about the nature of Indian sovereignty:

Our cases make clear that the Indians’ right to make their own laws and be governed by them *does not exclude all state regulatory authority on the reservation*. State sovereignty does not end at a reservation’s border. Though tribes are often referred to as “sovereign” entities, it was “long ago” that “the Court departed from Chief Justice Marshall’s view that ‘the laws of [a State] can have no force’ within reservation boundaries. *Worcester v. Georgia*, 6 Pet. 515, 561 (1832),” *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 141 (1980). [fn. om.] “Ordinarily,” it is now clear, “an Indian reservation is considered part of the territory of the State.” U.S. Dept. of Interior, *Federal Indian Law* 510, and n.1 (1958), citing *Utah & Northern R. Co. v. Fisher*, 116 U.S. 28 (1885); *see also Organized Village of Kake v. Egan*, 369 U.S. 60, 72 (1962).

29. *See, e.g., San Manuel*, 341 N.L.R.B. 138, 174 L.R.R.M. (BNA) 1489 (2004) (Schaumber dissenting).

30. *Hicks*, 533 U.S. at 360–61 (emphasis added).

31. *Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 148–49, 157–58 (1973).

32. *Salt River Pima-Maricopa Indian Cmty. v. Yavapai County*, 50 F.3d 739, 740 (9th Cir. 1995) (property tax); *Tunica-Biloxi Tribe v. Louisiana*, 964 F.2d 1536, 1542 (5th Cir. 1992) (sales tax on vehicle purchased for reservation use); *Organized Vill. of Kake v. Egan*, 369 U.S. 60, 75 (1962) (criminal laws, including fish and game laws).

That is not to say that States may exert the same degree of regulatory authority within a reservation as they do without. To the contrary, the principle that Indians have the right to make their own laws and be governed by them requires “an accommodation between the interests of the Tribes and the Federal Government, on the one hand, and those of the State, on the other.” *Washington v. Confederated Tribes of Colville Reservation*, 447 U.S. 134, 156 (1980); see also *id.*, at 181 (opinion of Rehnquist, J.). “When on-reservation conduct involving only Indians is at issue, state law is generally inapplicable, for the State’s regulatory interest is likely to be minimal and the federal interest in encouraging tribal self-government is at its strongest.” *Bracker, supra*, at 144. *When, however, state interests outside the reservation are implicated, States may regulate the activities even of tribe members on tribal land*, as exemplified by our decision on *Confederated Tribes*. In that case, Indians were selling cigarettes on their reservation to nonmembers from off-reservation, without collecting the state cigarette tax. We held that the State could require the Tribes to collect the tax from nonmembers, and could “impose at least ‘minimal’ burdens on the Indian retailer to aid in enforcing and collecting the tax,” 447 U.S. at 151. (Emphasis added).³³

Another aspect of Indian sovereignty is immunity from suit by states or individuals. Even where state law applies, Indian tribes may not be sued except when they have waived this immunity. This concept of sovereignty, however, also has come under severe attack from the Court itself, in *Kiowa Tribe of Oklahoma v. Manufacturing Technologies, Inc.*³⁴ Three dissenting justices would have discarded completely the doctrine of Indian immunity from state regulation.³⁵ The majority decided against doing so, now, but recognized that the doctrine serves no legitimate purpose when applied to commercial enterprises dealing with the world outside the reservation, and offered to Congress the first opportunity to eliminate or modify the doctrine. The Court stated:

The doctrine of tribal immunity came under attack as a few years ago in [*Oklahoma Tax Comm’n v. Citizen Band of Potawatomi Tribe of Oklahoma*, 498 U.S. 505 (1991)]. The petitioner there asked us to abandon or at least narrow the doctrine because tribal businesses had become far removed from tribal self-governance and internal affairs. We retained the doctrine, however, on the theory that Congress had failed to abrogate it in order to promote economic development and tribal self-sufficiency. *Potawatomi*, 498 U.S., at 510. The rationale, it must be said, can be challenged as inapposite to modern, wide-ranging tribal enterprises extending well beyond traditional tribal customs and activities. Justice Stevens, in a separate opinion, criticized tribal immunity as “founded upon an anachronistic fiction” and suggested it might not extend to off-reservation commercial activity. *Id.*, at 514–515 (concurring opinion).

33. *Hicks*, 533 U.S. at 362.

34. *Kiowa Tribe of Oklahoma v. Mfg. Tech., Inc.*, 523 U.S. 751 (1998).

35. *Id.* at 764–66.

There are reasons to doubt the wisdom of perpetuating the doctrine. At one time, the doctrine of tribal immunity from suit might have been thought necessary to protect nascent tribal governments from encroachments by States. In our interdependent and mobile society, however, tribal immunity extends beyond what is needed to safeguard tribal self-governance. This is evident when tribes take part in the Nation's commerce. Tribal enterprises now include ski resorts, gambling, and sales of cigarettes to non-Indians. See *Mescalero v. Jones*, 411 U.S. 145 (1973); *Potawatomi*, *supra*; *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44 (1996). In this economic context, immunity can harm those who are unaware that they are dealing with a tribe, who do not know of tribal immunity, or who have no choice in the matter, as in the case of tort victims.

These considerations might suggest a need to abrogate tribal immunity, at least as an overarching rule. Respondent does not ask us to repudiate the principle outright, but suggests instead that we confine it to reservations or to noncommercial activities. We decline to draw this distinction in this case, as we defer to the role Congress may wish to exercise in this important judgment.³⁶

III. Development of Labor and Employment Law in the Circuit Courts: The *Coeur D'Alene* Analysis

The federal courts have been called upon to determine whether various labor laws apply to tribal commercial enterprises located on reservation or trust lands. The Ninth, Seventh, Tenth, Second and Eleventh Circuits have adopted the same method of analysis and have ruled that OSHA, ERISA, FLSA, and ADA apply to these businesses. This line of cases began with *Donovan v. Coeur d'Alene Tribal Farm*.³⁷ Analysis begins with a presumption based on the following statement from *Federal Power Comm. v. Tuscarora Indian Nation* that "it is a principle now well settled by many decisions of the Supreme Court that a general statute in terms applying to all persons includes Indians and their property interests."³⁸ The Ninth Circuit proceeded to point out that in all of its previous decisions involving laws other than labor laws, it uniformly applied this presumption and held the laws applicable instead of interpreting them to exclude Indians.³⁹ The court observed, however, that there are three exceptions to the general rule:

(1) the law touches "exclusive rights of self-governance in purely intramural matters;" (2) the application of the law to the tribe would "abrogate rights guaranteed by Indian treaties;" or (3) there is proof "by legislative history or some other means that Congress intended [the law] not to apply to Indians or their reservations . . ." [*United States v. Farris*, 624 F.2d [890 (9th Cir. 1980)] at 893-94. In any of

36. *Id.* at 757-58.

37. *Donovan v. Coeur d'Alene Tribal Farm*, 751 F.2d 1113, 1114 (9th Cir. 1985).

38. *Fed. Power Comm. v. Tuscarora Indian Nation*, 362 U.S. 99, 116 (1960).

39. *Coeur d'Alene*, 751 F.2d at 1115-16.

these three situations, Congress must *expressly* apply a statute to Indians before we will hold that it reaches them.⁴⁰

The court applied these principles to the question whether OSHA applied to the Coeur d'Alene Tribal Farm.⁴¹ The farm was owned and operated by the tribe.⁴² It produced grain and lentils for the open market both within and outside Idaho.⁴³ Some of its workers were non-Indians, including the farm manager.⁴⁴ Its operations were like those of other farms owned by non-Indians.⁴⁵ The court found that OSHA's coverage is comprehensive and clearly included the farm. It then examined the exceptions from the general rule of applicability.⁴⁶ The tribe argued that the application of OSHA would infringe on its powers of self-government.⁴⁷ The court found that this proved far too much, for accepting it would mean that tribal enterprises would be exempt from virtually all federal laws, including tax laws that had already been held to apply.⁴⁸ The court concluded:

We believe that the tribal self-government exception is designed to except purely intramural matters such as conditions of tribal membership, inheritance rules, and domestic relations from the general rule that otherwise applicable federal statutes apply to Indian tribes.⁴⁹

The farm was obviously not a purely intramural matter for the tribe.

The operation of a farm that sells produce on the open market and in interstate commerce is not an aspect of tribal self-government. Because the Farm employs non-Indians as well as Indians, and because it is in virtually every respect a normal commercial farming enterprise, we believe that its operation free of federal health and safety regulations is neither profoundly intramural . . . nor essential to self-government.⁵⁰

The Tribe tried to persuade the court to adopt a formulation different than "purely intramural matter."⁵¹ It asserted that the self-government exception existed whenever the tribe would be deprived of a "fundamental aspect of sovereignty."⁵² It argued that one such aspect was its power to exclude non-Indians from its lands and that this power would be limited improperly if it were required to admit OSHA inspectors to

40. *Id.* at 1116.

41. *Id.* at 1114.

42. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. *Id.* at 1115.

47. *Id.* at 1116.

48. *Id.*

49. *Id.* (citations omitted).

50. *Id.* (citations omitted).

51. *Id.*

52. *Id.* at 1116-17.

its farm.⁵³ The court completely rejected the proposed formulation and the argument based on it.⁵⁴ The court acknowledged that the power of a tribe to exclude people from its land or to tax those who enter upon it is a hallmark of sovereignty, as held by the Supreme Court in *Merrion v. Jicarilla Apache Tribe*,⁵⁵ but pointed out that the *Merrion* case involved private citizens who were attempting to avoid tribal taxation and, consequently, the Court had no occasion to, and did not, suggest that Congress had to respect this sovereignty and could not modify it to require tribes to admit the government's own agents, such as OSHA inspectors, onto Indian lands.⁵⁶

The court then quickly dispensed with the second, "treaty rights" exception because the Coeur d'Alene Tribe had no treaty with the United States, and had no other agreement with the government that gave it any right to exclude anyone, including federal agents, from its reservation.⁵⁷ The court distinguished *Donovan v. Navajo Forest Products Industries*,⁵⁸ because that decision involved the Navajo, who had a treaty with a specific provision giving the tribe the right to exclude people other than tribe members from its reservation.⁵⁹ Finally, the third exception did not exist because there was nothing in the legislative history of OSHA suggesting a Congressional intent to exclude tribal enterprises from its scope.⁶⁰

The Ninth Circuit used its *Coeur d'Alene* analysis in two subsequent decisions. In *U.S. Department of Labor v. Occupational Safety & Health Review Commission*,⁶¹ the court once again addressed the question of the application of OSHA to tribal enterprises.⁶² In that case, the tribe owned and operated a sawmill on its reservation.⁶³ The finished products were sold in interstate commerce.⁶⁴ The majority of the mill

53. *Id.* at 1117.

54. *Id.*

55. 455 U.S. 130 (1982).

56. *Coeur d'Alene*, 751 F.2d at 1117.

57. *Id.*

58. 692 F.2d 709 (10th Cir. 1982).

59. *Coeur d'Alene*, 751 F.2d at 1117. In *Navajo Forest Products*, the court recognized and applied the *Tuscarora* rule. However, it found that OSHA did not apply to a wood products enterprise on the Navajo Reservation because one of the three exceptions described in *Coeur d'Alene* was applicable: where application of the law to the tribe would abrogate rights guaranteed by Indian treaties. *Id.* at 1116. The Navajo have a treaty that gives them the right to exclude non-Indians not authorized to enter upon the Navajo Reservation. The court in *Navajo Forest* decided that application of OSHA to the tribal enterprise would necessarily entail the presence of OSHA inspectors on the Reservation, whether or not authorized by the Navajo, in derogation of the treaty right. *Navajo Forest*, 692 F.2d at 712.

60. *Coeur d'Alene*, 751 F.2d at 1118.

61. 935 F.2d 182 (9th Cir. 1991).

62. *Id.* at 183.

63. *Id.*

64. *Id.*

workers were not Indians.⁶⁵ The mill was the largest source of income for the tribal government and almost all of the timber cut at the mill was supplied by tribal loggers.⁶⁶ Applying *Coeur d'Alene*, the court found that OSHA applied.⁶⁷ It ruled that the mill was a commercial enterprise and not a purely intramural matter, despite the fact that the mill's income was "critical to the tribal government."⁶⁸ The "treaty rights" exception was a more serious one: the tribe had a treaty with the United States that included a provision prohibiting any white person from residing on the reservation without permission.⁶⁹ Applying the canon of construction that treaty rights are to be liberally construed in favor of Indians, the court did not give a narrow interpretation to the word "reside."⁷⁰ It held that the tribe possessed a general right of exclusion.⁷¹ Nevertheless, the court had ruled that this right was not good against OSHA inspectors.⁷² It reasoned that OSHA gave inspectors a limited right of entry on private property and construed its earlier decisions as ruling implicitly that "the government was empowered to enforce the laws."⁷³ Accepting the tribe's argument that the treaty right gave it the power to exclude any and all federal agents as well as private citizens would mean that "the enforcement of nearly all generally applicable federal laws would be nullified, thereby effectively rendering the *Tuscarora* rule inapplicable to any Tribe which has signed a Treaty containing a general exclusion provision."⁷⁴ The court therefore rejected the argument and held that the treaty right of exclusion and the limited access of OSHA inspectors were not in conflict.⁷⁵

In *Lumber Industry Pension Fund v. Warm Springs Forest Products*, a case involving the same sawmill, the court held that ERISA applied to the mill.⁷⁶ The tribe had established a tribal pension plan for its members.⁷⁷ It transferred the tribe members working at the sawmill from a collectively bargained pension plan to the tribal plan and ceased making contributions to the former.⁷⁸ In the plan's suit to collect the unpaid contributions, the tribe argued that application of ERISA would strip it of its self-government powers.⁷⁹ The court disagreed.⁸⁰ It

65. *Id.*

66. *Id.*

67. *Id.* at 184.

68. *Id.*

69. *Id.*

70. *Id.* at 185.

71. *Id.*

72. *Id.* at 186.

73. *Id.*

74. *Id.* at 187.

75. *Id.*

76. 939 F.2d 683, 684 (9th Cir. 1991).

77. *Id.*

78. *Id.*

79. *Id.* at 685.

80. *Id.*

held that ERISA would not prevent the tribe from establishing its own plan.⁸¹ Instead, the law would only subject the tribe to monetary damages for breaching its obligations under the collectively bargained plan.⁸² It also found that there were no treaty rights that would be infringed by the application of ERISA and no evidence of congressional intent to exclude tribes or their enterprises from the coverage of ERISA.⁸³

Two years before *Lumber Industry Pension Fund*, the Seventh Circuit had followed *Coeur d'Alene* and reached the same conclusion regarding the application of ERISA.⁸⁴ The Chippewa tribe operated a health center on its reservation for the use of tribe members. It purchased from State Farm a health insurance policy for the workers at the center, including the plaintiff (who was a member of the tribe).⁸⁵ State Farm refused to pay a claim submitted by the plaintiff and the suit followed.⁸⁶ State Farm defended on the grounds that ERISA was the governing law and supplied a very high threshold for overturning a claims decision.⁸⁷ The court ruled that ERISA is a statute of general application.⁸⁸ It has exceptions for governmental plans but has no exceptions for Indian tribes or any plans they might adopt.⁸⁹ Following *Tuscarora* and *Coeur d'Alene*, the court found that ERISA was a comprehensive statute that was presumed to be applicable to the tribe's health insurance for its employees.⁹⁰ The Seventh Circuit then turned to the exceptions listed in *Coeur d'Alene*. The court found that the application of ERISA did not invade a purely intramural matter.⁹¹ ERISA, in its view, did not broadly and completely define the employment relationship between the tribe and its employees.⁹² It only applies if a tribe decides to offer an employment benefit plan, and then only imposes reporting, disclosure and fiduciary requirements.⁹³ Moreover, the plan was created by contract with a nontribal entity, State Farm.⁹⁴ The plaintiff also argued that the exemption given to federal and state governments in ERISA should be interpreted to include Indian tribes, too, because they are self-governing on their reservations.⁹⁵ This was rejected.⁹⁶

81. *Id.*

82. *Id.*

83. *Id.* at 685–86.

84. *Smart v. State Farm Ins. Co.*, 868 F.2d 929, 936 (7th Cir. 1989).

85. *Id.* at 930.

86. *Id.* at 930–31.

87. *Id.* at 931.

88. *Id.* at 933.

89. *Id.*

90. *Id.*

91. *Id.* at 935.

92. *Id.*

93. *Id.*

94. *Id.* at 936.

95. *Id.*

96. *Id.*

Finally, with respect to Smart's contentions that the exemptions provided for state and local governments indicate Congress' unwillingness to have ERISA apply to sovereigns generally, and thus Indian Tribes should also be similarly exempt, there is no clear evidence of congressional intent to exempt them. The analogy is particularly inapt given the significant differences between states and their political subdivisions on one hand and Indian Tribes on the other. *See Confederated Tribes of Warm Springs Reservation of Oregon v. Kurtz*, 691 F.2d 878, 880 (9th Cir. 1982) (distinguishing Tribes from States and their political subdivision); *United States v. Barquin*, 799 F.2d 619 (10th Cir. 1986) (refusing to hold that Indian Tribe was within ambit of "State or local government agency" as used in 18 U.S.C. § 666(c)). Significant concerns of federalism, peculiar to Federal-State relations, account for federal deference to the autonomy of State government. Federalism uniquely concerns States; there simply is no Tribe counterpart. Smart is unable to point to any evidence of congressional intent that ERISA is not applicable to Tribe employers and Indians.⁹⁷

The court found no "specific right" in the Chippewa Treaty that would interfere with the application of ERISA,⁹⁸ and as indicated in the above-quoted passage from its opinion, the court found no evidence of a congressional intent to exclude Tribes or Indians from the coverage of this law.⁹⁹

That same year, the Tenth Circuit Court of Appeals also adopted the *Coeur d'Alene* test.¹⁰⁰ The court found that 42 U.S.C. §§ 1981 and 2000d, laws prohibiting racial discrimination, were generally applicable laws.¹⁰¹ Applying the first *Coeur d'Alene* exception, however, the court found that these laws should not be applied to the facts at hand.¹⁰² Plaintiffs, descendants of the former slaves of the Cherokees, alleged that the Cherokees "have discriminated on the basis of race by refusing to accord them tribal membership and its privileges and benefits."¹⁰³ The court held, "[N]o right is more integral to a tribe's self-governance than its ability to establish its membership."¹⁰⁴ Because the application of the laws would intrude into this "purely intramural matter," the court did not exercise jurisdiction.¹⁰⁵

In *Reich v. Great Lakes Indian Fish & Wildlife Commission*, the Seventh Circuit considered the application of the Fair Labor Standards Act to game wardens employed by a commission formed by several tribes to enforce their members' treaty rights to fish and hunt on non-

97. *Id.*

98. *Id.* at 935.

99. *Id.* at 936.

100. *Nero v. Cherokee Nation of Oklahoma*, 892 F.2d 1457, 1462-63 (10th Cir. 1989).

101. *Id.* at 1462.

102. *Id.* at 1463.

103. *Id.*

104. *Id.*

105. *Id.*

reservation lands.¹⁰⁶ The majority and dissenting opinions agreed that employees of Indian agencies are covered by the FLSA.¹⁰⁷ The majority held, however, that because the wardens are armed law enforcement personnel, they come under FLSA's exemption of police officers.¹⁰⁸ The Ninth Circuit later came to the same conclusion with respect to the law enforcement officers of the Navajo Nation Division of Public Safety, an almost entirely Navajo police force that maintains law and order within the Navajo reservation, "a traditional governmental function."¹⁰⁹

The Second Circuit Court of Appeals joined the Ninth, Seventh, and Tenth Circuits in applying *Tuscarora* to federal labor and employment laws in *Reich v. Mashantucket Sand & Gravel*.¹¹⁰ The defendant was owned and operated by the Mashantucket Pequot, a tribe with a reservation but no treaty.¹¹¹ The company has both Indian and non-Indian employees.¹¹² It works exclusively on the reservation performing various construction jobs.¹¹³ These include the construction of roads and tribal homes, and also work on the continuing expansion of the Foxwoods High Stakes Bingo and Casino.¹¹⁴ The Foxwoods Casino is located on the reservation and is the principal source of income for the tribe.¹¹⁵ The question, once again, was whether OSHA applied to the company's operations.¹¹⁶ The Second Circuit held that it did, adopting and applying the *Coeur d'Alene* test.¹¹⁷ Accepting the established proposition that OSHA is a law of general applicability, the court considered whether any of the exceptions applied.¹¹⁸ The company "likened" itself to a department of public works," and claimed that OSHA would deprive it of its tribal sovereignty.¹¹⁹ It also argued that application of OSHA would prevent it from adopting its own safety rules. Both arguments were rejected.¹²⁰

The company claimed that its activities were purely intramural, because they were all performed on the reservation under the direction of the Tribal Council.¹²¹ The court found, however, that the company "is in the construction business; and its activities are of a commercial and service character, not a governmental character. That an entity is

106. 4 F.3d 490, 491 (7th Cir. 1993).

107. *Id.* at 495, 504.

108. *Id.* at 495.

109. *See generally* Snyder v. Navajo Nation, 382 F.3d 892 (9th Cir. 2004).

110. *See generally* 95 F.3d 174 (2d Cir. 1996).

111. *Id.* at 175.

112. *Id.*

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.* at 176.

117. *Id.* at 182.

118. *Id.* at 179.

119. *Id.*

120. *Id.*

121. *Id.* at 180.

owned by a tribe, operates as an arm of a tribe, or takes direction from a tribal council, does not ipso facto elevate it to the status of a tribal government.”¹²² The company’s admitted employment of non-Indians was very important to the court.

Limitations on tribal authority are particularly acute where non-Indians are concerned. See id. The Supreme Court has recognized that tribal “inherent sovereign powers . . . do not extend to the activities of nonmembers of the tribe.” *Montana*, 450 U.S. at 565, 101 S. Ct. at 1258; see also *A-1 Contractors v. Strate*, 76 F.3d 930, 939 (8th Cir. 1996). This is so because the “exercise of tribal power beyond what is necessary to protect tribal self-government or to control internal relations is inconsistent with the dependent status of the tribes. . . .” *Montana*, 450 U.S. at 564, 101 S. Ct. at 1258.

MSG’s employment of non-Indians weighs heavily against its claim that its activities affect rights of self-governance in purely intramural matters. In general, tribal relations with non-Indians fall outside the normal ambit of tribal self-government. Furthermore, intramural matters generally consist of conduct the immediate ramifications of which are felt primarily within the reservation by members of the tribe. *Cf. Farris*, 624 F.2d at 893 (intramural activities in the nature of conditions of tribal membership, domestic relations, and inheritance rules). Thus, the employment of non-Indians is another factor that tips the balance toward application of OSHA.¹²³

The final factor that caused the court to reject the company’s claim that application of OSHA would interfere with its sovereignty over purely intramural matters was that its construction work was not just on reservation roads and tribal homes but also on the expansion of the Foxwoods Casino, an enterprise indisputably involved in interstate commerce.¹²⁴ The court stated:

Indeed, “a bingo hall and casino [even on tribal grounds] designed to attract tourists from surrounding states undeniably affects interstate commerce. . . .” *United States v. Funmaker*, 10 F.3d 1327, 1331 (7th Cir. 1993) (citing *Katzenbach v. McClung*, 379 U.S. 294, 85 S. Ct. 377, 13 L. Ed. 2d 290 (1964)).¹²⁵

The court also quickly dismissed the company’s claim that OSHA would prevent it from adopting its own safety regulations.¹²⁶ The court pointed out that because tribes are *not* governments within the meaning of OSHA, OSHA’s preemption of state and local laws does not affect the tribes, who are therefore entitled to enact their own safety regulations (just like other employers under OSHA) as long as they are consistent

122. *Id.*

123. *Id.* at 180–81 (emphasis added).

124. *Id.* at 181.

125. *Id.*

126. *Id.*

with OSHA.¹²⁷ Because the Mashantucket Pequot have no treaty and because OSHA has no legislative history showing an intent to exclude Indian tribes or enterprises, these exceptions were not argued by the company.¹²⁸ The court concluded that the only possibly applicable exception, that for purely intramural matters, did not exist and the company's operations were subject to OSHA.¹²⁹

In 1999, the Eleventh Circuit joined the ranks of the courts of appeals using *Coeur d'Alene* analysis to determine the applicability of federal laws to on-reservation Indian-owned enterprises. In *Florida Paraplegic Association v. Miccosukee Tribe of Indians of Florida*,¹³⁰ the court held that a restaurant and entertainment facility operated by the Miccosukee Tribe was subject to the Americans with Disabilities Act (ADA).¹³¹ It found that the ADA is a law of general applicability, that the facility was not an intramural tribal function, that no treaty rights insulated the facility from federal law, and that the ADA has no exclusion of Indian tribes or their enterprises.¹³² But this was a suit by a private entity against the tribe.¹³³ Thus, even though ADA applied to the facility, the doctrine of tribal immunity from suit—which is distinct from the question whether substantive laws apply—meant that only the federal government could enforce the statute against the tribe.¹³⁴

The same thing happened in *Chayoon v. Chao*.¹³⁵ The plaintiff brought a claim against the Mashantucket Pequot, the owners of the giant Foxwoods Casino, under the Family and Medical Leave Act (FMLA).¹³⁶ The court held that the statute showed no sign that Congress intended to waive Indian tribes' immunity from suit.¹³⁷ The court did *not* say that the tribe was exempt from FMLA, only that it could not be enforced privately.¹³⁸ The plaintiff complained about the unfairness of this situation.¹³⁹ The court replied:

Foxwoods Resort Casino employs over 10,000 people and Native American gaming facilities are becoming more numerous throughout the country. Clearly, tribal sovereignty has the potential to deny many Americans employment benefits and rights that Congress has seen fit to extend to the private sector. See, e.g., *Garcia*, 268 F.3d at 85–86 (finding tribes immune from claims based on the Age Discrimination

127. *Id.*

128. *Id.* at 177.

129. *Id.* at 182.

130. 166 F.3d 1126 (11th Cir. 1999).

131. *Id.* at 1130.

132. *Id.* at 1129–30.

133. *Id.* at 1130.

134. *Id.* at 1135; see also *Kiowa*, 523 U.S. at 751.

135. 355 F.3d 141 (2d Cir. 2004).

136. 29 U.S.C. § 2601 et seq.; *Chayoon*, 355 F.3d at 142–43.

137. *Chayoon*, 355 F.3d at 143.

138. *Id.*

139. *Id.*

in Employment Act of 1967, § 2 et seq., as amended, 29 U.S.C.A. § 621 et seq.). While judges, as citizens, may be sympathetic to the plight of people like Mr. Chayoon, the courts are without authority to remedy the matter. Mr. Chayoon's remedy, if there is to be one, lies with Congress.¹⁴⁰

These cases manifest the recognition that as Indian tribes increasingly engage in business activities in commerce with people and business organizations from outside their reservations, there is no sound reason to treat them differently than non-Indian businesses. The courts of appeals have increasingly recognized this, as the cases discussed above demonstrate, and the Supreme Court has sounded the same theme. In other words, by the time the Board was presented with the *San Manuel* case, things had changed radically since the Board's decision in *Fort Apache*, both in terms of the nature and extent of Indian enterprises and in the judicial response to these developments.

IV. NLRB Law Catches Up With the Federal Courts

Many years ago, the Board held that a business is subject to the National Labor Relations Act even if it is located on an Indian reservation.¹⁴¹ It does not matter whether the employees of the business are Indians or not. *Texas-Zinc Minerals* involved a business that was not owned by the Indian tribe upon whose reservation it operated.¹⁴² In *Fort Apache Timber Company*,¹⁴³ the Board was faced for the first time with the question of whether to assert jurisdiction over a commercial enterprise owned and operated by an Indian tribe on its reservation.¹⁴⁴ The company was directed by the tribe's council, its governing body.¹⁴⁵ Because of the tribe's right of self-government on its reservation, the Board concluded that the exemption in the Act for state and local governments should be construed to include tribal government-owned businesses.¹⁴⁶

In *Devil's Lake Sioux Manufacturing Corporation*, the Board asserted jurisdiction over a manufacturing facility located on a reservation.¹⁴⁷ The business was owned by a corporation formed between the tribe and Brunswick Corporation. The tribe owned 51 percent of the stock and Brunswick owned 49 percent.¹⁴⁸ Despite the tribe's ownership of the majority interest of the corporation, the tribe did not direct

140. *Id.*

141. *Texas-Zinc Minerals Corp.*, 126 N.L.R.B. 602, 45 L.R.R.M. (BNA) 1356 (1960), *aff'd*, *Navajo Tribe v. NLRB*, 288 F.2d 162, 165 (D.C. Cir. 1961).

142. *Texas-Zinc*, 126 N.L.R.B. at 603, 45 L.R.R.M. (BNA) at 1356.

143. 226 N.L.R.B. 503, 93 L.R.R.M. (BNA) 1296 (1976).

144. *Id.* at 504.

145. *Id.*

146. *Id.* at 506.

147. 243 N.L.R.B. 163, L.R.R.M. 1380 (1979).

148. *Id.* at 163.

the workforce.¹⁴⁹ Instead, Brunswick officials were a majority on the corporation's board of directors and Brunswick set labor relations policy at the facility.¹⁵⁰ Because the corporation was "not a *wholly* owned tribal enterprise which [was] *completely* controlled by the tribal council," it was not exempt as an arm of a government.¹⁵¹

Next, in *Southern Indian Health Council, Inc.*, the Board followed *Fort Apache* in refusing to assert jurisdiction over a tribal health facility owned and operated by a consortium of tribes on a reservation in San Diego, California.¹⁵² There was no reference in the Board's opinion to *Tuscarora*, *United States v. Wheeler*, *Montana v. Blackfeet Tribe*, or any of the Supreme Court decisions establishing the rules concerning the exercise of federal jurisdiction on Indian reservations. There was no reference to the *Coeur d'Alene* decision that intervened between *Fort Apache* and *Southern Indian Health Council*. There is no evidence in either *Fort Apache* or *Southern Indian Health Council* that the Board was even aware of the governing federal law.

That changed dramatically four years later in *Sac and Fox Industries, Ltd.*, which clearly presaged *San Manuel*.¹⁵³ The Board adopted the *Coeur d'Alene* analysis.¹⁵⁴ It did so even though it recognized that the *Coeur d'Alene* test was "developed in cases involving Indian or tribal activities on the reservation" and the business before it was located off the tribe's reservation.¹⁵⁵

The Board started with the *Tuscarora* presumption of applicability, because

there is little question that the NLRA is a statute of general applicability. Like various other Federal employment-related statutes which have been held to be of general applicability, [fn. om.] the NLRA's jurisdictional definitions of "employer," "employee" and "commerce" are of "broad and comprehensive scope," [fn. om.] containing only a few specified exemptions. Nowhere in the list of exemptions or elsewhere in the statute is there any mention of Indians or their off-reservation enterprises. [fn. om.] Thus, the *Tuscarora* rule clearly applies, and contrary to the result in *Fort Apache* and *Southern Indian Health Council* in which the tribal enterprises were located on the reservation, we cannot conclude in this case that SFI is exempt from the coverage of the Act at its Commerce [Oklahoma] facilities merely because those facilities are owned and controlled by the Tribe.¹⁵⁶

149. *Id.*

150. *Id.*

151. *Id.* at 164 (emphasis added).

152. 290 N.L.R.B. 436, 436-437, 129 L.R.R.M. 1013 (1988).

153. 307 N.L.R.B. 241, 140 L.R.R.M. 1054 (1992) (*SFI*).

154. *Id.* at 243.

155. *Id.* at 244 n.20.

156. *Id.* at 243. See section 2(2), (3), and (6) of the Act. The only exemptions specified in section 2(2)'s definition of "employer" are "the United States or any wholly owned Government corporation, or any Federal Reserve Bank, or any State or political subdivision thereof, or any person subject to the Railway Labor Act . . . or any labor organi-

Next, the Board considered the exceptions listed in *Coeur d'Alene*.¹⁵⁷ It decided that application of the Act would not interfere with the tribe's right to self-government in "purely intramural matters."¹⁵⁸ The facility in question was a manufacturing operation and the majority of its workforce was composed of people who were not tribal members.¹⁵⁹ The Board pointed out that the Act does not "broadly and completely define the relationship between [an employer] and its employees," but simply provides the means for workers to organize and to create a collective bargaining relationship, without compelling any agreement or the substantive terms of any agreement.¹⁶⁰ Finally, the Act does not "regulate purely intramural matters such as Tribal membership, inheritance rules, or domestic relations."¹⁶¹

The Sac and Fox nation had numerous treaties with the federal government. There was no "specific provision," however, in any of these treaties that would be abrogated by application of the Act.¹⁶² Turning to the last exemption, the Board ruled:

SFI has not referred us to, and we are not aware of, any discussion whatsoever in the legislative history of the NLRA dealing with Indians. Nor is there any basis in the language of the Act itself for inferring a Congressional intent to exempt Indians or their off-reservation tribal enterprises. . . . Further, even if true, as our dissenting colleague would read it, that *Fort Apache* did in fact hold that all enterprises owned by governmental entities are exempt from the Act wherever they do business, this holding was implicitly overruled less than a year later with the Board decided to assert jurisdiction over foreign-government instrumentalities that do business within the territorial jurisdiction of the United States. [fn. om.] . . . The Act's exemption in Sec. 2(2) for a "political subdivision" of a "State" does not clearly include an off-reservation enterprise. Accordingly, we find that application of the NLRA to SFI in this proceeding would not be contrary to Congressional intent.¹⁶³

The Board distinguished *Fort Apache* and *Southern Indian Health Council* but studiously avoided endorsing the continued vitality of the holdings in those cases.¹⁶⁴ The reasoning in *SFI* was completely incompatible with those earlier decisions, which were based on the notion that an Indian tribe is a "government" within the mean of section 2(2)

zation (other than when acting as an employer), or anyone acting in the capacity of officer or agent of such labor organization." *Id.*

157. *Id.* at 243–44.

158. *Id.* at 244.

159. *Id.*

160. *Id.*

161. *Id.*

162. *Id.*

163. *Id.* at 245; See *State Bank of India*, 229 NLRB 838 (1977). See also *State Bank of India*, 262 N.L.R.B. 1108 (1982); *State Bank of India*, 273 N.L.R.B. 267 (1984), *enforced*, 808 F.2d 526 (7th Cir. 1986).

164. *SFI*, 307 N.L.R.B. at 243 n.14.

of the Act. “Nowhere in the list of exemptions or elsewhere in the statute is there any mention of Indians or their off-reservation enterprises.”¹⁶⁵ It is equally true that there is no mention of *on*-reservation enterprises. “The Act’s exemption in Sec. 2(2) for a political subdivision of a ‘State’ does not clearly include an off-reservation tribal enterprise.”¹⁶⁶ Section 2(2) does not clearly include an *on*-reservation tribal enterprise. Thus, the reasons given by the Board why off-reservation businesses wholly owned and controlled by an Indian tribe are not exempt as a part of a government exempt under section 2(2) apply with equal force to *on*-reservation businesses.

In its last decision in this area before *San Manuel, Yukon Kusko-kwim Health Corporation*, a three-member panel of the Board upheld the decision of the NLRB regional director in Alaska to direct an election among the employees of a hospital in Alaska operated by and for Alaska Natives.¹⁶⁷ The Board agreed that the hospital was subject to its jurisdiction because it is not on reservation land and most of the employees are not Indian.¹⁶⁸

The hospital tried to distinguish *SFI* on the grounds that the business in that case was an ordinary manufacturing enterprise, whereas the hospital is set up to serve the Alaska Natives themselves. The Board decided that this difference was not important. The Board distinguished *Indian Health Council* on the grounds that the hospital in that case was on reservation land, whereas the hospital in *Yukon* is not and that most of the employees in the *Southern Indian Health Council* case were members of Indian tribes, but the *Yukon* employees are predominantly non-Indian.

The Board in *Yukon* also took a view of what is a “reservation” that was quite restrictive. The land on which the hospital is located is not technically reservation land. There is only one reservation in Alaska. The federal government owns the land and building used by the hospital. The hospital is run by a nonprofit corporation whose directors are elected by the membership of the Alaskan tribes located in the area served by the hospital, pursuant to a compact with the federal government, which had originally operated the facility under the Indian Health Services. The hospital’s operations continue to be funded by the federal government. It is located in a Native Region established under federal law, and serves the native population. The Native Region is not a reservation, however. The land within it is not protected by federal law from being sold to non-Natives, and this was the point relied upon

165. *Id.* at 243.

166. *Id.* at 245.

167. 328 N.L.R.B. 761 (1999).

168. *Id.*

by the Board to find that the land in question should not be regarded as a reservation or its equivalent.

The Board was not faced with the question whether it could or should exert jurisdiction over on-reservation, Indian-owned businesses, and so it did not rule on this subject or even make a direct statement of its current views. Instead, whenever it addressed the distinction between on-reservation and off-reservation businesses, it did so in carefully crafted passages that left room for a change in the policy adopted in *Fort Apache*. For example, *Southern Indian Health Council* was not distinguished solely on the grounds that the hospital in that case was on a reservation. If that were all that mattered, it would have been the only distinguishing factor cited. Instead, the Board further distinguished the earlier case on the grounds that most of the employees in the hospital involved in that case were Native American, whereas in *Yukon*, only one or two out of the 40 to 44 employees were Alaska Natives, a “factor favoring application of the Act.” This reduces the importance of whether businesses are on or off a reservation from the status of a test in and of itself (as it was in *Fort Apache*) to the status of one factor in the analysis whether to apply the Act.

When the Board in *Yukon* described its earlier holding in *SFI*, it said, “the Board held that since the NLRA is a statute of general applicability, in the absence of certain specific exemptions, it applies to all persons including Indians and, at least, *Indians’ off-reservation* property interests.”

The holding in *Yukon* further undermined the vitality of the *Fort Apache*-type analysis. The *Fort Apache* reasoning was very simple and straightforward: Indian tribes are sovereign governments and therefore exempt under the NLRA’s exemption for state and local governments. The hospital in *Yukon* was owned by a nonprofit corporation governed by a board of directors elected by the Alaska Native tribes located in the area served by the hospital. That nonprofit corporation took over operation of the hospital from the federal Indian Health Services pursuant to a self-determination compact with the federal government. Under *Fort Apache*, this enterprise would have been regarded as part of tribal government, and therefore exempt. In fact, that is exactly what happened in *Southern Indian Health Council*. As mentioned, one of the ways the Board distinguished *Southern Indian Health Council* was that the hospital was located on reservation land, but the actual decision in *Southern Indian Health Council* laid no emphasis on this point, instead resting on the theory that tribal operations are government operations and therefore exempt. At the end of its decision in *Yukon*, the Board explicitly rejected the contention that Indian-owned enterprises are “government” operations and therefore exempt. Although it confined this ruling to the case before it, involving an off-

reservation operation, *Yukon Kuskokwim* showed that the Board had not retreated from *SFT*'s effective abandonment of *Fort Apache*.

Its order, however, was denied enforcement by the Court of Appeals for the District of Columbia Circuit.¹⁶⁹ While the court agreed that an Indian tribe is not a "state" within the meaning of Section 2(2) of the Act, and found no fault with the Board's use of the distinction between enterprises on a reservation or off, it returned the case to the Board for further exploration of the hospital's claim that it was part of the U.S. government pursuant to the Indian Self-Determination Act, 25 U.S.C. § 450, et seq. (ISDA).¹⁷⁰ The Board's supplemental decision was issued at the same time as *San Manuel*.¹⁷¹ The Board continued to reject the ISDA argument but applied the completely new analytical framework of *San Manuel* and reversed itself on the question of jurisdiction over the hospital. Instead of inquiring whether or not the operation was on a reservation, it applied the "governmental versus proprietary" distinction, familiar from many other contexts, and came to the unsurprising decision that because the hospital functioned as the public hospital for the Alaska Natives in the Yukon-Kuskokwim Delta area, and did not serve the non-Native population and was not in competition with any private hospitals, it was governmental in character. The differences between such a hospital and a casino like *San Manuel* are so stark and pervasive that the pairing of these two cases should give all practitioners good guidance for predicting future cases involving Indian enterprises, even though the Board will be proceeding case by case.¹⁷²

V. IGRA and NLRB Jurisdiction

The Board in *San Manuel* rejected the argument that whatever jurisdiction it had was divested by the Indian Gaming Regulatory Act, 25 U.S.C. §§ 2701 et seq. The Board pointed out that IGRA regulates gaming but the LMRA does not, and the LMRA regulates labor relations but "IGRA does not address labor relations—the only aspect of the Respondent's business with which the Board is concerned."¹⁷³ The U.S. Court of Appeals for the Ninth Circuit considered the labor relations aspects of IGRA in *In re Gaming Related Cases*.¹⁷⁴ At issue were

169. *Yukon Kuskokwim Health Corp. v. NLRB*, 234 F.3d 714, 718 (D.C. Cir. 2000).

170. *Id.* at 717–18.

171. *Yukon Kuskokwim Health Corp.*, 341 N.L.R.B. No. 139, __ L.R.R.M. __ (2004).

172. See *San Manuel*, slip op. at 9. There will be gray areas, of course. *Yukon Kuskokwim* can be compared with *NLRB v. Chapa De Indian Health Program, Inc.*, 316 F.3d 995, 1000 (9th Cir. 2003), a subpoena enforcement action where the court determined that a financially independent, nonprofit tribal health services organization, which contracted to provide services to the tribe as well as others and operated outside a reservation, was not clearly exempt from the LMRA because of its commercial nature. *Id.*

173. *Id.*, slip op. at p. 10.

174. 331 F.3d 1094 (2003), cert. denied, *Coyote Valley Band of Pomo Indians v. California*, 540 U.S. 1179 (2004).

the negotiations for a gaming compact between the State of California and tribes in California desiring to operate casinos.¹⁷⁵ Under IGRA, slot machines and table games may be included in Indian casino offerings only under a compact between the tribe and the State in which the casino is located.¹⁷⁶ IGRA requires the state to negotiate the compact in good faith.¹⁷⁷ Several California tribes claimed that the state had negotiated in bad faith by insisting on provisions requiring tribes with casinos to share their profits with poor, nongaming tribes and to adopt a model “Tribal Labor Relations Ordinance” (TLRO) that guaranteed tribal casino employees the right to organize for collective bargaining.¹⁷⁸

The court held in favor of the state on all issues.¹⁷⁹ It concluded that the state had not negotiated in bad faith under IGRA.¹⁸⁰ The court decided the TLRO issue on the grounds that IGRA allows the state to negotiate on any subject that is “directly related to the operation of gaming activities.”¹⁸¹ Without employees, there would be no gaming activities, and furthermore, the state has a legitimate interest in their conditions since most of them are non-Indian residents of the state.¹⁸² The court also decided that the state did not bargain in bad faith by insisting on the terms of the model TLRO because it gives only “modest organizing rights,” it was negotiated largely by the tribes and union representatives, and it has been accepted by most of the tribes.¹⁸³

Thus, although IGRA itself is not concerned with labor relations, gaming compacts between tribal employers and the states where their casinos are located may include provisions about labor relations. One of the more interesting areas of the intersection of labor and Indian law will be the development of the relationship of NLRB jurisdiction to rules of employer and union conduct established in gaming compacts—a species of State conduct that is not either regulatory or proprietary.

VI. Next? Antidiscrimination Laws

Beyond the issue of the NLRB’s jurisdiction, possible further erosion of the insulation of tribal enterprises from the federal labor and employment law is foreseeable. Although most such laws have been held to apply to Native American-owned businesses on reservation land, the notable exception has been the antidiscrimination laws. Title

175. *Id.* at 1095.

176. *Id.* at 1097.

177. *Id.*

178. *Id.* at 1110.

179. *Id.*

180. *Id.*

181. *Id.* at 1115 (quoting 25 U.S.C. § 2710(d)(3)(C)(vii)).

182. *Id.* at 1116.

183. *Id.*

VII of the Civil Rights Act of 1964 has been held not to apply.¹⁸⁴ I believe there is a question, however, whether the exemption in 42 U.S.C. § 2000e(b) for “Indian tribes” is just for the tribes internally or for all of their enterprises, including those that are fully engaged in interstate commerce, employing mostly non-Indians and serving non-Indian customers. It does not make any sense for Indian tribes as employers to be privileged to engage in race, sex, religious, and other forms of discrimination, including harassment, against non-Indian employees and applicants for employment. These cases did not involve large-scale businesses employing mostly non-Indians and selling to non-Indian clientele. The legislative history shows that the intent of the exclusion was to protect Indian businesses employing their own members.¹⁸⁵ Where discrimination cases are presented that involve businesses like the San Manuel casino, it is possible that the federal courts will revisit the question whether Title VII applies with more in-depth consideration.

On the other hand, it is likely that the Age Discrimination in Employment Act (ADEA) will be held to apply to Indian businesses like casinos, despite the current state of the law. In *E.E.O.C. v. Cherokee Nation*,¹⁸⁶ the court relied on the “abrogation of treaty rights” exception in *Coeur d’Alene* to find the Age Discrimination in Employment Act not applicable to the Cherokee Nation.¹⁸⁷ There was a dissent by Judge Tacha, the author of the opinion in *Dille*, who would have found the ADEA applicable because it does not exclude Indian tribes explicitly.¹⁸⁸ In *E.E.O.C. v. Fond du Lac Heavy Equipment and Construction Co., Inc.*,¹⁸⁹ the court recognized the *Tuscarora* rule, but found the ADEA inapplicable on the particular facts because the dispute was “a strictly internal matter.”¹⁹⁰ The court explained:

The dispute is between an Indian applicant and an Indian tribal employer. The Indian applicant is a member of the tribe, and the business is located on the reservation. Subjecting such an employment relationship between the tribal member and his tribe to federal control and supervision dilutes the sovereignty of the tribe. The consideration of a tribe member’s age by a tribal employer should be allowed to be restricted (or not restricted) by the tribe in accordance with its culture and traditions. Likewise, disputes regarding this issue should be allowed to be resolved internally within the tribe. Federal regulation of the tribal employer’s consideration of age in determining

184. *Dille v. Council of Energy Resource Tribes*, 801 F.2d 373, 374 (10th Cir. 1986) (express exclusion from definition of “Employer”); *Wardle v. Ute Indian Tribe*, 623 F.2d 670, 672 (10th Cir. 1980); *Dawavendewa v. Salt River Project Agric. Imp.*, 276 F.3d 1150, 1159 n.9 (9th Cir. 2002); *Garcia v. Akwesasne Hous. Auth.*, 268 F.3d 76, 88 (2d Cir. 2001).

185. 110 CONG. REC. 13701-13702 (June 13, 1964).

186. 871 F.2d 937 (10th Cir. 1989).

187. *Id.* at 938 n.3.

188. *Id.* at 942 (Tacha dissenting).

189. 986 F.2d 246 (8th Cir. 1993).

190. *Id.* at 248.

whether to hire a member of the tribe to work in the business located on the reservation interferes with an intramural matter that has traditionally been left to the tribe's self-government.¹⁹¹

The court did not find the tribe generally exempt from the ADEA, but just that "the ADEA does not apply to the narrow facts of this case which involve a member of the tribe, the tribe as an employer, and on the reservation employment . . ." ¹⁹² Despite the narrowness of the decision, there was a dissent that would have followed Judge Tacha's reasoning in *E.E.O.C. v. Cherokee Nation*, and four other judges of the circuit voted for rehearing en banc.¹⁹³

The same kind of narrow approach was taken in *E.E.O.C. v. Karuk Tribe Housing Authority*.¹⁹⁴ The ADEA was held not to apply to a tribe member's complaint that he was terminated from the Karuk Tribe Housing Authority due to his age.¹⁹⁵ The court saw this as "an intramural dispute between the tribal government and a member of the tribe."¹⁹⁶

Because the ADEA is a statute of general applicability and contains no express exclusion of either Indian tribes or their businesses, it should be anticipated that in future cases, it will be held applicable to "proprietary," commercial enterprises such as casinos.

191. *Id.* at 249.

192. *Id.* at 251.

193. *Id.*

194. 260 F.3d 1071 (9th Cir. 2001).

195. *Id.* at 1080.

196. *Id.* at 1081.

Implications of *Smith v. City of Jackson* on Equal Pay Act Claims and Sex-Based Pay Discrimination Claims Under Title VII

William E. Doyle Jr.

In *Smith v. City of Jackson*,¹ a plurality of the Supreme Court held that disparate impact claims are actionable under the Age Discrimination in Employment Act (ADEA). A noteworthy aspect of the plurality's reasoning is found in a footnote discussion of the Equal Pay Act:

We note that if Congress intended to prohibit all disparate-impact claims, it certainly could have done so. For instance, in the Equal Pay Act of 1963, 29 U.S.C. § 206(d)(1), Congress barred recovery if a pay differential was based “on any other factor”—reasonable or unreasonable—“other than sex.” The fact that Congress provided that employees [*sic*] could use only *reasonable* factors in defending a suit under the ADEA is therefore instructive.²

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1. *Id.* 125 S. Ct. 1536 (2005).

2. *Smith*, 125 S. Ct. at 1544, n.11 (Stevens, J., joined by Souter, Ginsburg, and Breyer, JJ.) (emphasis in original). It is an interesting question whether this footnote discussion is nonbinding dictum. The Court has stated that “[w]hen an opinion issues for the Court, it is not only the result but also those portions of the opinion necessary to that result by which we are bound.” *Seminole Tribe v. Fla.*, 517 U.S. 44, 66 (1996). The holding in *Smith* was that the ADEA permits claims based on the disparate impact theory of discrimination. *Smith*, 125 S. Ct. at 1540. In reaching this holding, the Court considered the fact that the ADEA contains a “reasonable factor other than age” (RFOA) defense. *Id.* at 1543–44 (Stevens, J.) & 1551–52 (O'Connor, J., concurring in the judgment). The plurality determined that the RFOA confirms Congress's intent to permit disparate impact claims under the ADEA, because otherwise the RFOA would serve no purpose. *Id.* at 1543–44. Footnote 11 appears immediately after the plurality's discussion of the purpose of the RFOA:

It is, accordingly, in cases involving disparate-impact claims that the RFOA provision plays its principal role by precluding liability if the adverse impact was attributable to a nonage factor that was “reasonable.” Rather than support an argument that disparate impact is unavailable under the ADEA, the RFOA provision actually supports the contrary conclusion. *Id.* at 1544.

Footnote 11 reinforces the plurality's reasoning about the legislative purpose for the RFOA by providing contrasting text that Congress used to “prohibit all disparate impact claims.” *Id.* at 1544 n.11. Whether this discussion was strictly necessary to the plurality's conclusion may be questioned. Nonetheless, the footnote 11 contrast clearly supported a

The clear implications of this brief discussion are that disparate impact claims are not cognizable under the Equal Pay Act (EPA) and that the EPA's "any other factor other than sex" affirmative defense can be sustained by a factor that is "reasonable or unreasonable."³ There have been circuit splits on these very issues under the Equal Pay Act and, through the Bennett Amendment, under Title VII with respect to sex-based pay discrimination claims. Thus, the plurality's discussion of the

central aspect of the plurality's reasoning upon which the Court's holding was based. Because it was not merely a passing reference, the question of whether footnote 11 was strictly necessary to the plurality's reasoning may not be crucial to its precedential value, since the courts of appeals generally feel themselves bound even by the Court's "considered dicta." See, e.g., *Oyebanji v. Gonzales*, 418 F.3d 260, 264–65 (3d Cir. 2005); *Crowe v. J.P. Bolduc*, 365 F.3d 86, 92 (1st Cir. 2004); *United States v. Marlow*, 278 F.3d 581, 588 n.7 (6th Cir. 2002); *Batjac Prods., Inc. v. Goodtimes Home Video Corp.*, 160 F.3d 1223, 1232 (9th Cir. 1998); *Gaylor v. United States*, 74 F.3d 214, 217 (10th Cir. 1996); *City of Timber Lake v. Cheyenne River Sioux Tribe*, 10 F.3d 554, 557 (8th Cir. 1993); *McCoy v. Mass. Inst. of Tech.*, 950 F.3d 13, 19 (1st Cir. 1991); *Nichol v. Pullman Standard, Inc.*, 889 F.2d 115, 120 n.8 (7th Cir. 1989).

3. *Smith*, 125 S. Ct. at 1544, n.11. In a concurring opinion, Justice Scalia did not join in the part of the plurality's opinion quoted in the text above, but he wrote "I agree with all of the Court's reasoning" in that part. *Smith*, 125 S. Ct. at 1546. The Court has held that "[w]hen a fragmented Court decides a case and no single rationale explaining the result enjoys the assent of five Justices, the holding of the Court may be viewed as that position taken by those Members who concurred in the judgment on the narrowest grounds." *Grutter v. Bollinger*, 539 U.S. 306, 325 (2003) (quoting *Marks v. United States*, 490 U.S. 188, 193 (1977)). Because Justice Scalia expressly agreed with the plurality's reasoning, there are five Justices who assent to a single rationale explaining the Court's holding. *Smith*, 125 S. Ct. at 1546.

Justice Scalia did not join in the plurality's opinion because he would defer to an EEOC regulation that, in his view, interpreted the ADEA as permitting disparate impact claims. *Id.* In the context of the EPA, the EEOC has issued regulations interpreting the EPA, but they do not address the issues discussed by the plurality in footnote 11 in *Smith*. See 29 C.F.R. §§ 1620.1–1620.34 (2005); 51 Fed. Reg. 29819–26 (Aug. 20, 1986).

As described in the text below, the EEOC has issued a compliance manual chapter that addresses these issues. EEOC Compliance Manual on "Compensation Discrimination," EEOC Directive No. 915.003 (Dec. 5, 2000). However, it is not clear that Justice Scalia would defer to the EEOC compliance manual. For one, as noted below, many of the implications of the plurality's footnote 11 involve Title VII and the Court has already determined on several occasions that EEOC interpretations of the substantive provisions of Title VII are not entitled to *Chevron*-level deference because Congress did not authorize the EEOC to promulgate rules or regulations pursuant to Title VII. See *National Railroad Passenger Corp. v. Morgan*, 536 U.S. 101, 111 n.6 (2002); *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 257 (1991); *Gen. Elec. Co. v. Gilbert*, 429 U.S. 125, 141 (1976). Moreover, the EEOC's compliance manual simply notes the circuit split on these issues and states the EEOC's view favoring one side of the split. EEOC Compliance Manual on "Compensation Discrimination," EEOC Directive No. 915.003 (Dec. 5, 2000), at §§ 10-III.B. n.34 & 10-IV.F.2. & nn.65–66. In his dissent in *Mead*, Justice Scalia noted concern over the prospect of an agency interpretation effectively overturning, through the administrative deference doctrine, a prior judicial interpretation of a statute. *United States v. Mead Corp.*, 533 U.S. 218, 248–49 (2001) (Scalia, J., dissenting) ("I know of no case, in the entire history of the federal courts, in which we have allowed a judicial interpretation of a statute to be set aside by an agency—or have allowed a lower court to render an interpretation of a statute subject to correction by an agency."); see also *Nat'l Cable & Telecomm. Ass'n v. Brand X Internet Servs.*, 125 S. Ct. 2688 (2005) (Scalia, J., dissenting) ("Article III courts do not sit to render decisions that can be reversed or ignored by Executive officers.").

Equal Pay Act's "any other factor other than sex" defense has significant implications.⁴

This short comment examines four of these implications:

- (1) There has been a circuit split on whether the EPA's "any other factor" affirmative defense can be sustained by literally any factor or only by factors meeting a standard of reasonability. The plurality appears to have resolved this split in favor of the circuits that adopted the literal interpretation of "any other factor."⁵
- (2) All circuits that have addressed the issue have required the employer to establish that the asserted factor was the actual cause of the challenged pay disparity, and have afforded the plaintiff an opportunity to establish that the employer's asserted legitimate cause is a pretext for discrimination. Because the reasonableness of the factor has a significant bearing on both causation and pretext, it is unclear how the plurality's discussion modifies the doctrinal framework for determining these issues.
- (3) The Bennett Amendment of Title VII incorporates the EPA's affirmative defenses into Title VII with respect to sex-based pay discrimination claims. Therefore, the implications of the plurality's discussion carry over into Title VII as well. A major implication is that the disparate impact theory is ruled out as a basis for sex-based pay discrimination claims under Title VII.
- (4) Under the plurality's reasoning, the "any other factor" affirmative defense may present a headwind to class certification of sex-based pattern or practice pay discrimination claims under Title VII. Under the plurality's broad interpretation, the affirmative defense may be sustained by factors that are unique to each particular putative class member. Where the employer offers evidence of such unique factors, determinations about the affirmative defense will require individual mini-trials, making class treatment unmanageable.

I. "Any" Means Literally Any

The courts of appeals have been split on whether the "any other factor other than sex" defense of the Equal Pay Act (EPA) can be read

4. Justice White, joined by Chief Justice Rehnquist and Justice O'Connor, dissented from a denial of *certiorari* in *Randolph Central School District v. Aldrich*, in which the issue was "whether, under the federal Equal Pay Act, an employer seeking to establish the factor-other-than-sex defense must prove that the factor is supported by a legitimate business-related reason." *Randolph Cent. Sch. Dist. v. Aldrich*, 506 U.S. 965, 965 (1992). The dissent explained the significant differences of opinions among the circuits on this issue and the related issues under Title VII, but did not indicate the dissenters' view of the correct outcome. *Id.*

5. *Smith*, 125 S. Ct. at 1544, n.11 (quoting 29 U.S.C. § 206(d)(1)).

literally to mean *any* factor. Several courts of appeals have held, and the EEOC has agreed, that the “any other factor” defense is not to be read literally and must be constrained by a rule of reasonability: only factors other than sex that are reasonably related to legitimate business interests will sustain the defense.⁶ Other courts of appeals have favored a literal interpretation: “any” means any.⁷ Thus, footnote 11 of the *Smith* plurality opinion casts doubt on the continued validity of the holdings of those circuits that require the employer to offer a reasonable business purpose to establish the “any other factor other than sex” affirmative defense.⁸

6. See *Steger v. Gen. Elec. Co.*, 318 F.3d 1066, 1078–79 (11th Cir. 2003) (“Because the evidence showed that the salary retention plan was justified by ‘special exigent circumstances connected with the business,’ and because there was no evidence which rebutted GE’s explanation, the district court did not err in submitting the matter to the jury or in denying Steger’s motion for judgment as a matter of law.”) (quoting *Irby v. Bittick*, 44 F.3d 949, 954 (11th Cir. 1995)); *Belfi v. Prendergast*, 191 F.3d 129, 136 (2d Cir. 1999) (“Further, to successfully establish the ‘factor other than sex’ defense, an employer must also demonstrate that it had a legitimate business reason for implementing the gender-neutral factor that brought about the wage differential.”); *Aldrich v. Randolph Cent. Sch. Dist.*, 963 F.2d 520, 525–26 (2d Cir. 1992) (“Without a job-relatedness requirement, the factor-other-than-sex defense would provide a gaping loophole in the statute through which many pretexts for discrimination would be sanctioned. . . . For these reasons, we hold that an employer bears the burden of proving that a bona fide business-related reason exists for using the gender-neutral factor that results in a wage differential in order to establish the factor-other-than-sex defense.”); *Glenn v. Gen. Motors Corp.*, 841 F.2d 1567, 1571 (11th Cir. 1988) (“[T]he ‘factor other than sex’ exception applies when the disparity results from unique characteristics of the same job; from an individual’s experience, training, or ability; or from special exigent circumstances connected with the business.”); *Kouba v. Allstate Ins. Co.*, 691 F.2d 873, 876 (9th Cir. 1982) (“The Equal Pay Act concerns business practices. It would be nonsensical to sanction the use of a factor that rests on some consideration unrelated to business. An employer thus cannot use a factor which causes a wage differential between male and female employees absent an acceptable business reason.”); EEOC Compliance Manual on “Compensation Discrimination,” EEOC Directive No. 915.003 (Dec. 5, 2000), at § 10-IV.F.2. & nn.65–66 (“An employer asserting a ‘factor other than sex’ defense also must show that the factor is related to job requirements or otherwise is beneficial to the employer’s business. Moreover, the factor must be used reasonably in light of the employer’s stated business purpose as well as its other practices.”).

7. See *Dey v. Colt Constr. & Dev. Co.*, 28 F.3d 1446, 1462 (7th Cir. 1994) (“We explained in *Fallon* that the EPA’s fourth affirmative defense ‘is a broad catch-all exception [that] embraces an almost limitless number of factors, so long as they do not involve sex.’ The factor need not be ‘related to the requirements of the particular position in question,’ nor must it even be business-related.”) (quoting *Fallon v. State of Illinois*, 882 F.2d 1206, 1208 (7th Cir. 1989) [internal citations omitted]); *cf.* *Taylor v. White*, 321 F.3d 710, 719 (8th Cir. 2002) (noting in context of a sex-based pay discrimination claim under Title VII: “In conducting this examination, our concern is not related to the wisdom or reasonableness of the asserted defense. It is related solely to the issue of whether the asserted defense is based on a ‘factor other than sex.’”).

8. Since *Smith*, two courts of appeals have reaffirmed the circuit split on this issue, but neither court discussed or even referenced *Smith*. See *Wernsing v. Dep’t of Human Servs.*, 427 F.3d 466, 470 (7th Cir. 2005) (“The disagreement between this circuit (plus the eighth) and those that required an ‘acceptable business reason’ is established, and we are not even slightly tempted to change sides.”); *Balmer v. HCA, Inc.*, 423 F.3d 606, 612 (6th Cir. 2005) (“The Equal Pay Act’s catch-all provision ‘does not include literally

II. Determining Causation and Pretext If the Factor Can Be Unreasonable?

In addition to the circuit split on whether “any factor” means literally any factor, *Smith* footnote 11 appears to cast doubt on several other, related aspects of this affirmative defense. Even in circuits that adopt the more literal reading of “any,” the reasonableness of the factor plays a significant role. For example, even in these “literal” circuits, if the employer is able to offer sufficient evidence that, if believed, would sustain the affirmative defense, the plaintiff then is afforded an opportunity to establish that the employer’s justification is a pretext for sex discrimination.⁹ Of course, one of the ways a plaintiff may establish pretext is to show that the factor was unreasonable under the circumstances.¹⁰

If, as the *Smith* footnote 11 suggests, the affirmative defense may be established even where the factor is unreasonable, the traditional pretext analysis that is part of the framework for assessing the affirmative defense must be substantially modified. Moreover, in many cases the evidence will support competing inferences about the actual cause of the pay disparity, and courts typically submit such questions to the jury for determination, if each of the inferences is at least reasonable.¹¹ If the justification itself can be unreasonable, one wonders how the court is to determine whether an inference from the evidence is reasonable and how the jury is to be instructed about determining whether the factor was the actual cause of the pay disparity. Perhaps the jury is to be instructed that the employer must prove that the factor is the actual cause of the pay disparity, but that the reasonableness of the factor cannot be considered in determining whether the employer has met its burden of proof on this issue.

any other factor, but a factor that, at a minimum, was adopted for a legitimate business reason,” quoting *EEOC v. J.C. Penney Co.*, 843 F.2d 249, 253 (6th Cir. 1988).

9. *Cf. Strecker v. Grand Forks County Soc. Serv. Bd.*, 640 F.2d 96, 101 n.2 (8th Cir. 1981) (“Arguably, the education and experience requirements could be a pretext for sex discrimination, however, plaintiff introduced no evidence that this was Central Personnel’s intent when it established these criteria.”).

10. *See Kouba*, 691 F.2d at 876–77 (“Even with a business-related requirement, an employer might assert some business reason as a pretext for a discriminatory objective. . . . A pragmatic standard, which protects against abuse yet accommodates employer discretion, is that the employer must use the factor reasonably in light of the employer’s stated purpose as well as its other practices.”).

11. *See Lawrence v. CNF Trans.*, 340 F.3d 486, 494–95 (8th Cir. 2003) (“This court has recognized that experience with a company may constitute a factor in the salary calculation. Notwithstanding that consideration, we believe the jury was entitled to weigh this evidence against the size of the raises given [to the plaintiff’s comparators]” (citations omitted)); *Price v. Lockheed Space Operations Co.*, 856 F.2d 1503, 1506 (11th Cir. 1988) (“[T]he evidence *in toto* presents two competing inferences, that the appellees discriminated on the basis of sex, and that there existed a reason other than sex for the continuing wage disparity. It is the function of the jury as the traditional finder of facts, and not the court, to resolve the conflict between these competing inferences.”).

As significantly, some courts have ruled that a factor may not be the basis for the affirmative defense if the factor has a disparate impact based on sex.¹² However, the *Smith* plurality is straightforward in saying that disparate impact claims are not cognizable under the EPA, and that the “any other factor other than sex” language is precisely the text Congress used to “prohibit” disparate impact claims under the EPA.¹³

III. The Disparate Impact Theory Is Not Available for Sex-Based Pay Discrimination Claims Under Title VII

This discussion about footnote 11’s impact on EPA claims also has significant implications for sex-based Title VII compensation discrimination claims. The “Bennett Amendment,” contained in section 703(h) of Title VII, provides that “[i]t shall not be an unlawful employment practice under [Title VII] for any employer to differentiate upon the basis of sex in determining the amount of the wages or compensation paid or to be paid to employees of such employer if such differentiation is authorized by the provisions of [the Equal Pay Act].”¹⁴ The Supreme Court has held that the Bennett Amendment incorporates the affirmative defenses of the EPA into Title VII.¹⁵ The Court in *Gunther* had expressed doubt as to whether sex-based, disparate impact pay discrimination claims are viable under Title VII in light of the Bennett Amendment and the EPA’s “any other factor” defense:

More importantly, incorporation of the fourth affirmative defense could have significant consequences for Title VII litigation. Title VII’s prohibition of discriminatory employment practices was intended to be broadly inclusive, proscribing “not only overt discrimination but also practices that are fair in form, but discriminatory in operation.” *Griggs v. Duke Power Co.*, 401 U.S. 424, 431, 91 S. Ct. 849, 853, 28 L. Ed. 2d 158 (1971). The structure of Title VII litigation, including presumptions, burdens of proof, and defenses, has been designed to reflect this approach. The fourth affirmative defense of the Equal Pay Act, however, was designed differently, to confine the application of the Act to wage differentials attributable to sex discrimination. H.R. Rep. No. 309, 88th Cong., 1st Sess., 3 (1963), U.S. Code Cong. & Admin. News 1963, p. 687. Equal Pay Act litigation, therefore, has been structured to permit employers to defend against charges of discrimination where their pay differentials are based on a bona fide use of “other factors other than sex.”¹⁶

Running parallel to the EPA discussion above, several courts of appeals have held, and the EEOC has agreed, that the “any other fac-

12. *See Dey*, 28 F.3d at 1462 (“Because it is not our province to second-guess the employer’s business judgment, we ask only whether the factor is bona fide, whether it has been discriminatorily applied, and in some circumstances, whether it may have a discriminatory effect” (citations omitted; emphasis added)).

13. *Smith*, 125 S. Ct. at 1544 n.11.

14. 42 U.S.C. § 2000e-2(h) (2005).

15. *County of Washington v. Gunther*, 452 U.S. 161, 171 (1981).

16. *Id.* 452 U.S. at 170 [footnote omitted].

tor” defense applicable to Title VII through the Bennett Amendment does not foreclose sex-based, disparate impact pay discrimination claims under Title VII.¹⁷

Other courts of appeals have disagreed that sex-based disparate impact pay discrimination claims are viable under Title VII in light of the Bennett Amendment.¹⁸ Thus, a major implication of the Court’s discussion is that it precludes disparate impact theories as a basis for liability in sex-based pay discrimination claims under Title VII.¹⁹

If the *Smith* footnote 11 implies that the disparate impact theory is unavailable under Title VII with respect to sex-based pay discrimination claims, presumably this forecloses claims based on the “alternative employment practice” component of the disparate impact theory developed by the courts and codified by the Civil Rights Act of 1991.²⁰ Moreover, plaintiffs in disparate impact claims have been afforded an

17. See *Aldrich*, 963 F.2d at 528 (“In order to establish a valid claim under Title VII for sex-based wage discrimination, a plaintiff can demonstrate a disparate impact from use of a facially neutral employment practice . . .”); *EEOC v. J.C. Penney Co.*, 843 F.2d 249, 253 (6th Cir. 1988) (“In our circuit, however, the Bennett Amendment cannot constitute a blanket bar to all claims of wage discrimination based on disparate impact because the ‘factor other than sex’ defense does not include literally any other factor, but a factor that, at a minimum, was adopted for a legitimate business reason.”); *Kouba*, 691 F.2d at 876 (“An employer thus cannot use a factor which causes a wage differential between male and female employees absent an acceptable business reason.”); EEOC Compliance Manual on “Compensation Discrimination,” EEOC Directive No. 915.003 (Dec. 5, 2000), at § 10-III.B. n. 34 (“Enforcement staff should be aware that questions have been raised regarding the availability of the disparate impact theory in sex-based compensation discrimination cases. . . . The Commission’s view is that the disparate impact method of proof is available for sex-based compensation discrimination under Title VII.”).

18. See, e.g., *Taylor v. White*, 321 F.3d 710, 719 (8th Cir. 2002) (“In conducting this examination, our concern is not related to the wisdom or reasonableness of the asserted defense. It is related solely to the issue of whether the asserted defense is based on a ‘factor other than sex.’”); *Mullin v. Raytheon Co.*, 164 F.3d 696, 702 (1st Cir. 1999) (reading *Gunther* as precluding disparate impact theory in EPA and sex-based Title VII pay discrimination cases); *Colby v. J.C. Penney Co.*, 811 F.2d 1119, 1127 (7th Cir. 1987) (The Bennett Amendment “seems to imply, and the Supreme Court in [*Gunther*], assumed, that a disparate impact . . . is not a ground for challenging a practice that is within the scope of the amendment.”).

19. Compare *Carlson v. C.H. Robinson Worldwide, Inc.*, No. 02-3780, 2005 WL 758602, at *7, *16 (D. Minn. Mar. 31, 2005) (certifying class for sex-based pay discrimination claim under disparate impact theory), and *Hnot v. Willis Group Holdings Ltd.*, 228 F.R.D. 476, 486 (S.D.N.Y. 2005) (same), and *Anderson v. Boeing Co.*, 222 F.R.D. 521, 542 (N.D. Okla. 2004) (same), and *Jarvaise v. Rand Corp.*, 212 F.R.D. 1, 2 (D.D.C. 2002) (same), with Defendant Rand Corporation’s Amended Reply Memorandum in Support of its Motion for Summary Judgment on Plaintiffs’ Class Claim of Pay Discrimination Under Title VII or, Alternatively, for Decertification of the Class, *Jarvaise v. Rand Corp.*, No. 1:96-CV-02680 (RWR/JMF), at 14–15 (D.D.C. filed June 15, 2004) (arguing that plaintiffs’ disparate impact pay discrimination claim under Title VII is precluded by the Bennett Amendment).

20. See, e.g., *Kovacevich v. Kent State Univ.*, 224 F.3d 806, 831 (6th Cir. 2000) (in evaluating plaintiff’s sex-based disparate impact pay discrimination claim under Title VII, district court erred in not determining whether “there exists an alternative employment practice that would achieve the same business ends with a less discriminatory impact”).

opportunity to establish that the employer's asserted business justification was a pretext for discrimination.²¹ It is unclear what modifications must be made to this framework to accommodate the permissible reliance on unreasonable factors other than sex. Perhaps the jury is to be instructed that it must find that employer actually relied on the asserted "factor other than sex," but that it may not consider the reasonableness of the factor in making this determination. This may be an instruction that will be difficult for the jury to understand and implement. As Justice O'Connor noted in her concurrence in judgment in *Smith*, "[r]eliance on an unreasonable factor would indicate that the employer's explanation is, in fact, no more than a pretext for *intentional* discrimination."²²

IV. The Plurality's Discussion Suggests a Challenge to Class Certification of Sex-Based Pay Discrimination Claims Under Title VII

The plurality's broad interpretation of the "any other factor" defense suggests it will be more difficult to secure class certification of sex-based pay discrimination claims under Title VII. There are a host of factors—such as qualitative aspects of education and experience typically not included in statistical evidence of a pattern or practice of discrimination—that would sustain the affirmative defense if the factor need not meet any reasonableness standard. Where the employer intends to offer evidence of factors unique to particular employees, this may make it difficult for plaintiffs to establish that that "there are questions of law or fact common to the class" or that their "claims . . . are typical of the claims . . . of the class" as required by Rule 23(a) of the Federal Rules of Civil Procedure.²³ Moreover, determination of the merits of the "any other factor" defense where the employer offers evidence of factors unique to particular employees may require individual mini-trials, making the action unmanageable in a class format.

A. *Affirmative Defenses and Class Certification*

The "any other factor" affirmative defense has seldom been considered by the courts in the context of class certification. The only case

21. *Id.* (district court erred in not considering whether the plaintiff showed "that the employer's reason was a pretext for discrimination"); *Kouba*, 691 F.2d at 876 ("Even with a business-related requirement, an employer might assert some business reason for a discriminatory objective.")

22. *Smith*, 125 S. Ct. at 1552 (citing *Reeves v. Sanderson Plumbing Prods., Inc.*, 530 U.S. 133, 147 (2000); *Hazen Paper Co. v. Biggins*, 507 U.S. 604, 613–14 (1993) [emphasis in original]).

23. FED. R. CIV. P. 23(a)(2) & (3). Commonality and typicality are hotly contested in sex-based pay discrimination cases under Title VII. *See, e.g.*, *Grosz v. Boeing Co.*, 2005 WL 1515070, at *1 (9th Cir. June 28, 2005) (approving district court's denial of class certification based on plaintiffs' failure to demonstrate commonality and typicality); *Carlson*, 2005 WL 758602, at *8–10, *14–15 (rejecting employer's arguments that plaintiffs failed to establish commonality and typicality and certifying class of salaried employees).

available through Westlaw that addressed a challenge to class certification based on the Bennett Amendment did not involve the “any other factor” defense.²⁴ In *Radmanovich v. Combined Insurance Co.*, the plaintiffs alleged that the employer discriminated against its female employees with regard to hiring, promotions, and commission opportunities, and that the employer created, fostered, and permitted a sexually hostile work environment.²⁵ The plaintiffs sought certification of a class of “[a]ll women who . . . were sales agents or managers at some point during their employment with Combined.”²⁶ Combined Insurance argued in its memorandum in opposition to class certification that unique defenses precluded a finding that the representative plaintiffs’ claims were typical of the class claims. In particular, Combined argued that “the pay . . . claims of each class member would be subject to the defenses created by the Bennett Amendment, which specifies there is no violation of Title VII if an employer bases compensation on productivity (as Combined does with commissions).”²⁷ The court rejected this argument, explaining that “[t]ypicality under Rule 23(a) should be determined with reference to the company’s actions, not with respect to particularized defenses it might have against certain class members.”²⁸

In other contexts, the courts of appeals have considered affirmative defenses in determining whether to certify a class under Rule 23 of the Federal Rules of Civil Procedure.²⁹ The majority of circuits that have considered this issue have held that affirmative defenses should be taken into account when assessing class certification, but the fact that such defenses involve individualized inquiries does not categorically rule out certification.³⁰ As it did in *Radmanovich*, the majority rule

24. See *Radmanovich v. Combined Ins. Co.*, 216 F.R.D. 424, 438 n.6 (N.D. Ill. 2003).

25. *Id.* at 428.

26. *Id.* at 430.

27. Combined’s Memorandum in Opposition to Plaintiff’s Motion for Class Certification, at 8–9; *Radmanovich v. Combined Ins. Co.*, No. 01-C-9502 (N.D. Ill. filed June 5, 2003).

28. *Radmanovich*, 216 F.R.D. at 433 (quoting *Wagner v. NutraSweet Co.*, 95 F.3d 527, 534 (7th Cir. 1996)).

29. See, e.g., *In re Monumental Life Ins. Co. Litig.*, 365 F.3d 408, 420–21 (5th Cir. 2004); *Gunnells v. Healthplan Servs., Inc.*, 348 F.3d 417, 434, 438 (4th Cir. 2003); *Allapattah Servs., Inc. v. Exxon Corp.*, 333 F.3d 1248, 1260–61 (11th Cir. 2003) (unrelated holding affirmed in *Exxon Mobil Corp. v. Allapattah Servs., Inc.*, 125 S. Ct. 2611 (2005)); *Smilow v. Southwestern Bell Mobile Sys., Inc.*, 323 F.3d 32, 39–40 (1st Cir. 2003); *In re Linerboard Antitrust Litig.*, 305 F.3d 145, 162 (3d Cir. 2002); *In re Visa Check/Mastermoney Antitrust Litig.*, 280 F.3d 124, 138 (2d Cir. 2001).

30. See *In re Monumental Life Ins. Co. Litig.*, 365 F.3d at 421 (“Though individual class members whose claims are shown to fall outside the relevant statute of limitations are barred from recovery, this does not establish that individual issues predominate, particularly in the face of defendants’ common scheme of fraudulent concealment.”); *Allapattah Servs.*, 333 F.3d at 1261 (“[T]he real question for the district court was whether the common issue of liability dominated over the individual issues raised by Exxon’s affirmative defenses. . . . [i]n similar situations numerous courts have recognized that the presence of individualized damages issues does not prevent a finding that the common issues in the case predominate.”); *Smilow*, 323 F.3d at 40 (“Courts traditionally have been

would appear to limit the effectiveness of the “any other factor” affirmative defense as a means of opposing class certification.

However, there are several reasons to believe that this line of authority does not preclude an argument against class certification based on the “any other factor” affirmative defense. First, most of the cases involved procedural defenses to liability, such as statutes of limitations.³¹ Second, several of the cases involved affirmative defenses, such as mitigation, which do not address liability, but affect only the scope of the remedy.³²

By contrast, the Bennett Amendment is a substantive provision of Title VII under which reliance on a factor that establishes the “any other factor” defense is positively declared *not* to be “an unlawful employment practice.”³³ This is an affirmative immunity from substantive liability, not a procedural immunity like a statute of limitations or a limit on the scope of relief like a mitigation defense. Indeed, the Supreme Court has held that section 703(h) of Title VII, which contains the Bennett Amendment, “delineates which employment practices are illegal and thereby prohibited and which are not.”³⁴ Thus, the “any other factor” defense is not the typical affirmative defense that excuses otherwise established liability. Rather, it is an express exemption from the statutory definition of the practices that constitute “unlawful employment practices.” This has significant implications for placement of the “any other factor” defense within the framework for pattern or practice cases under Title VII.

reluctant to deny class action status under Rule 23(b)(3) simply because affirmative defenses may be available against individual members.”); *In re Linerboard Antitrust Litig.*, 305 F.3d at 162 (“However, most courts have refused to deny class certification simply because there will be some individual questions raised during the proceedings.”); *In re Visa Check/Mastermoney Antitrust Litig.*, 280 F.3d at 138 (“Although a court must examine the relevant facts and both the claims and defenses in determining whether a putative class meets the requirements of Rule 23(b)(3), the fact that a defense ‘may raise and may affect different class members differently does not compel a finding that the individual issues predominate over common ones.’” (quoting *Waste Mgmt. Holdings, Inc. v. Mowbray*, 208 F.3d 288, 296 (1st Cir. 2000)). *But see Gunnells*, 348 F.3d at 438 (“[W]e have flatly held that ‘when defendants’ affirmative defenses . . . may depend on facts peculiar to each plaintiff’s case, class certification is erroneous.’” (quoting *Broussard v. Meineke Discount Muffler Shops, Inc.*, 155 F.3d 331, 342 (4th Cir. 1998)).

31. *See In re Monumental Life Ins. Co. Litig.*, 365 F.3d at 420–21 (statute of limitations defense); *Smilow*, 323 F.3d at 40 (waiver defense); *In re Linerboard Antitrust Litig.*, 305 F.3d at 162 (statute of limitations defense); *Waste Mgmt. Holdings, Inc.*, 208 F.3d at 295–96 (statute of limitations defense); *Wagner v. NutraSweet Co.*, 95 F.3d 527, 534 (7th Cir. 1996) (release of claims defense).

32. *See In re Visa Check/Mastermoney Antitrust Litig.*, 280 F.3d at 138 (mitigation of damages defense); *Allapattah Servs.*, 333 F.3d at 1261 (set-off claims characterized as affirmative defenses “which pertained primarily to the issues of damages rather than liability”).

33. 42 U.S.C. § 2000e-2(h) (2005).

34. *Franks v. Bowman Transp. Co.*, 424 U.S. 747, 759 (1976); *see also Int’l Brotherhood of Teamsters v. United States*, 431 U.S. 324, 346 (1977).

B. *The “Any Other Factor” Defense and the Teamster’s Framework for Pattern or Practice Cases Under Title VII*

As noted, courts have only infrequently entertained challenges to class certification based on the “any other factor” defense. Thus, there has been little discussion of where the “any other factor” defense is considered within the *Teamsters* framework for pattern or practice claims under Title VII.

Recall that the Supreme Court has said that pattern or practice cases typically will be tried in two phases.³⁵ First, there is a liability phase in which the plaintiffs must “establish by a preponderance of the evidence that . . . discrimination was the company’s standard operating procedure—the regular rather than the unusual practice.”³⁶ During this liability phase, the plaintiffs attempt to establish a prima facie case of a pattern or practice of discrimination, typically by offering statistical evidence supported by anecdotal evidence of individual instances of discrimination.³⁷ If the plaintiff is able to establish a prima facie case, the burden of production shifts to the employer to meet the prima facie showing by demonstrating that the plaintiffs’ proof is either inaccurate or insignificant.³⁸ In this first phase, because the plaintiffs typically use statistical analyses as “proof of the expected result of a regularly followed discriminatory policy . . . the employer’s burden is to provide a nondiscriminatory explanation for the apparently discriminatory result.”³⁹ However, there are no “particular limits on the type of evidence the employer may use” to meet this burden of production.⁴⁰

If the plaintiff is successful in convincing the trier of fact that the employer has engaged in a pattern or practice of disparate treatment, then the court may enter an order for declaratory and/or injunctive relief.⁴¹ However, if the plaintiffs seek individual relief, then the action moves to the second phase under this *Teamsters* framework.⁴² The second phase of the pattern or practice action focuses on the remedy and the district court “must usually conduct additional proceedings . . . to determine the scope of individual relief.”⁴³ During this second, remedial phase, the burden rests on the employer to demonstrate that the challenged employment action with respect to the individual was based on legitimate, nondiscriminatory reasons.⁴⁴

35. *Teamsters*, 431 U.S. at 359–62.

36. *Id.* at 336.

37. *Id.* at 337–41, 361–62 n.20.

38. *Id.* at 360.

39. *Id.* at 360 n.46.

40. *Id.*

41. *Id.* at 361.

42. *Id.*

43. *Id.*

44. *Id.* at 362.

There is a surface appeal to placing the “any other factor” affirmative defense into phase two of the *Teamsters* framework, as the employer bears the burden of persuasion under the affirmative defense just as it bears the burden of demonstrating in phase two that the individual class members were not subject to the pattern or practice of discrimination found in phase one. However, the Court has held that section 703(h) is not directed toward the remedial aspects of Title VII.⁴⁵ Rather, as noted above, the Court has held that the “any other factor” defense is directed to the definition of what constitutes an “unlawful employment practice” under Title VII.⁴⁶ Moreover, it would appear altogether inappropriate to allow the pattern or practice *finding*—in contrast perhaps to evidence that the plaintiff used to establish a pattern or practice—to influence whether the employer has established the affirmative defense.⁴⁷ Allowing the pattern or practice *finding* to influence the determination about the “any other factor” affirmative defense seems particularly inappropriate where that finding is based largely on statistical evidence that omits the very types of factors, such as qualitative aspects of education or experience, that may establish the affirmative defense.

Indeed, in *Teamsters* itself, the Court did not allow the pattern or practice finding to influence its determination of the applicability of a provision of Section 703(h) that immunizes bona fide seniority systems from liability under Title VII. In particular, the Court determined that the plaintiffs’ statistical and anecdotal evidence was sufficient to sustain the district court’s conclusion that the employer engaged in a pattern or practice of disparate treatment against minority candidates for line driver positions.⁴⁸ Nonetheless, despite the pattern or practice finding, the Court determined that the employer’s seniority system was “entirely bona fide,” and rejected the Government’s contention that the seniority system could not be bona fide because it perpetuated the discriminatory effects of pre-Act discrimination.⁴⁹

Thus, from a doctrinal perspective, the “any other factor” defense is appropriately considered within phase one of the *Teamster’s* framework, notwithstanding the surface appeal of phase two placement,

45. *Franks*, 424 U.S. at 760.

46. *Id.*

47. See *Teamsters*, 431 U.S. at 362 (“[A]s is typical of Title VII pattern-or-practice suits, the question of individual relief does not arise until it has been proved that the employer has followed an employment policy of unlawful discrimination. The force of that proof does not dissipate at the remedial stage of the trial.”).

48. *Id.* at 336–43.

49. *Id.* at 353–55. It is also noteworthy that the Court considered and resolved the government’s challenge to the impact of the employer’s seniority system as part of the discussion of liability, and prior to turning to remedial issues. *Id.* Thus, the Court’s own ordering suggests that determinations under section 703(h) must take place within phase one of the *Teamster’s* framework. *Id.*

which derives from the fact that the employer bears the burden of persuasion to establish the “any other factor” defense.

C. *The “Any Other Factor” Defense and Class Certification in Recent Sex-Based Pay Discrimination Cases Under Title VII*

If individualized hearings are required to make determinations as to the “any other factor” defense, this presents a significant impediment to class certification. Even courts that are generally receptive to class certification in Title VII cases have appreciated that individual-specific “mini-trials” would make class treatment unmanageable. For example, in *Carlson v. C.H. Robinson Worldwide, Inc.*,⁵⁰ the plaintiffs sought class certification for a variety of discrimination claims, including a sex-based pay discrimination claim under Title VII. The district court certified a subclass consisting of “all females who have been employed on a full-time basis by [the employer] in a domestic branch office at any time during the liability period.”⁵¹ However, the court limited the certification to issues of liability and declaratory and injunctive relief under Rule 23(b)(2), deferring consideration of the plaintiffs’ motion to certify the subclass for monetary damages under Rule 23(b)(3) until after liability is determined.⁵² The court noted that the plaintiffs’ “request for lost wages, nominal damages and punitive damages necessitates a second, remedial phase of the litigation that is separate from resolution of their claim for injunctive relief.”⁵³ The court deferred its ruling on class certification of the remedial phase of the action because it was particularly troubled by the nature of the determinations required in that phase: “Importantly, these damages inquiries require individualized factual determinations whose manageability could overwhelm the litigation.”⁵⁴

Similarly, in *Beck v. Boeing*,⁵⁵ the district court certified a class action in which the plaintiffs alleged a pattern or practice of compensation and promotion discrimination. As to the liability phase of the action, the district court certified a class under Rule 23(b)(2).⁵⁶ The court rejected Boeing’s argument that the class would be unmanageable due to “an endless litany of fact-specific inquiries into the circumstances of each class member” and explained:

Nor do we find that certifying a class in this matter need result in a parade of countless individual plaintiffs explaining the circumstances of their complaints. Plaintiffs’ theory of the case is premised on their

50. 2005 WL 758602, at *8–10, *14–15 (D. Minn. Mar. 31, 2005).

51. *Id.*

52. *Id.*

53. *Id.* at *16.

54. *Id.*

55. 203 F.R.D. 459, 466 (W.D. Wash. 2001), *aff’d in pertinent part*, 60 Fed. Appx. 38, 39 (9th Cir. 2003).

56. *Id.* at 467.

ability to prove that, at the highest levels of the corporation, Boeing knew that systemic gender-based discrimination was occurring and did nothing (or did not do enough) to put an end to it. Liability will hinge on that proof and the punitive damages assessed against defendants (if any) will flow from that finding.⁵⁷

As to the damages phase of the action, the court considered class certification under Rule 23(b)(3).⁵⁸ The court noted that “[t]he spectre of ‘individualized hearings’ raises its head in two ways in the context of this litigation”: (1) “by the possibility of a defense rebuttal . . . wherein a defendant[] . . . bring[s] forth evidence showing non-discriminatory reasons for its actions” and (2) “by the possibility of demonstrating the defendant’s conduct in specific instances in pursuit of either back pay or punitive damages.”⁵⁹ Although the court downplayed these concerns—noting that the Ninth Circuit permits formula relief in pattern or practice cases to “avoid ‘a quagmire of hypothetical judgments’ or the strain of a multitude of separate fact-finding hearings”—and certified a class for punitive damages, the court nonetheless refused to certify the class for back pay under Rule 23(b)(3):

The Court is at a loss to fashion a method of arriving at [back pay] damages for the plaintiffs and class members without individualized hearings into the specific circumstances of each person’s employment and what the discrimination to which they have been subjected (if such is proven) has cost them over the time period allotted to the class. For this portion of the damages request, a class action is not the superior method by which to fairly and economically resolve the issue and that portion of plaintiffs’ lawsuit will not be certified as a class action.⁶⁰

The Ninth Circuit affirmed the district court’s decision to certify a class under Rule 23(b)(2) for liability purposes, but vacated the district court’s decision to certify a class for punitive damages under Rule 23(b)(3).⁶¹ However, the Ninth Circuit agreed with the district court that “Boeing cannot defeat class certification at the liability phase by arguing that it is entitled to introduce individualized evidence that each of its employment decisions was motivated by a legitimate non-discriminatory reason.”⁶²

In another prominent sex-based compensation discrimination case under Title VII, *Dukes v. Wal-Mart Stores, Inc.*,⁶³ Wal-Mart argued that

57. *Id.* at 466.

58. *Id.* at 467.

59. *Id.* [citations omitted].

60. *Id.*

61. *Beck*, 60 Fed. Appx. at 39–40.

62. *Id.* at 39.

63. 222 F.R.D. 137, 186–87 (N.D. Cal. 2004). The Ninth Circuit granted the parties’ cross-petitions for permission to appeal the district court’s June 22, 2004 order granting class certification. Oral arguments in the appeals (Nos. 04-80057, 04-16688) were heard on August 8, 2005. *Id.*

the action would be unmanageable in both the liability and remedy stages due to the massive size of the proposed class.⁶⁴ The district court agreed that manageability was an important consideration:

[T]he Court agrees that it must very carefully assess the manageability of issues presented by this unique case. While courts possess wide discretion to flexibly respond to manageability issues that may arise during the course of a class action, this court must be confident that such issues will not be of such a magnitude as to defy its ability to oversee this case in a responsible and reasonable manner.⁶⁵

With respect to liability, the court cited Wal-Mart's argument that "due process" would necessarily require 3,244 individual mini-trials, including testimony from 3,244 Store Managers, to determine whether each individual Wal-Mart store discriminated against class members employed by that store.⁶⁶ The court rejected this argument, explaining that "the evidence introduced during Stage I should properly focus on matters relevant to the class as a whole, such as statistical analysis and evidence of system-wide policies and practices."⁶⁷ The court concluded that Wal-Mart "is not . . . entitled to circumvent or defeat the class nature of the proceeding by litigating whether every individual store discriminated against individual class members."⁶⁸

As to remedy, Wal-Mart asserted an argument similar to the "any other factor" defense in an attempt to demonstrate that class treatment would be unmanageable. In particular, Wal-Mart argued that class certification was improper because the Civil Rights Act of 1991 limits the remedies available to a plaintiff where the employer demonstrates that it would have taken the same employment action in the absence of the impermissible motivating factor.⁶⁹ The court rejected this argument, reasoning that the employer is afforded such an opportunity only in "mixed motives" cases and that the plaintiffs in *Dukes* had opted to proceed only under a single-motive theory of discrimination.⁷⁰ Nonetheless, the court acknowledged that "holding individual hearings for the number of women potentially entitled to backpay in this case is impractical on its face . . ."⁷¹

Thus, courts certainly recognize that individualized assessments make the action unmanageable in a class format. Courts favorably disposed to class certification have avoided the manageability problem by ruling that individualized assessments are not required to determine

64. *Dukes*, 222 F.R.D. at 173. The parties estimated that the proposed class exceeds 1 million current and former female Wal-Mart employees. *Id.* at 144.

65. *Id.*

66. *Id.* at 173–74.

67. *Id.* at 174.

68. *Id.*

69. *Id.* at 186–87.

70. *Id.*

71. *Id.* at 176.

liability.⁷² However, these courts did not consider the “any other factor” affirmative defense under the Bennett Amendment of Title VII. As discussed above, there are compelling grounds for individualized assessments of the “any other factor” defense during the liability phase.⁷³ Where the employer raises the “any other factor” defense, and offers evidence of factors unique to particular employees, the court must entertain mini-trials to allow the jury to determine whether the employer’s evidence establishes the affirmative defense. Moreover, the “any other factor” affirmative defense does not depend on the nature of the plaintiff’s allegations, and, therefore, plaintiffs could not modify their claims to preclude the employer from offering individualized proof in support of this defense. It is to be seen whether the “any other factor” defense proves to be a successful basis for opposing class certification in sex-based pay discrimination claims under Title VII.

72. *See supra* text accompanying notes 49–67.

73. *See supra* text accompanying notes 45–49.

Pounding Square Pegs into Round Holes: Noncompete Agreements for Temporary Employees Stand Existing Law on Its Head

William E. Pilchak*

I. Introduction

Acme's board of directors decides to switch staffing company vendors. The successful bidder is notified, the new contract signed, and the outgoing supplier given the bad news. The transition starts smoothly. But soon the "temps" inform Acme that their departing employer has asserted noncompete agreements signed during the application process. They are forbidden from serving Acme on behalf of another company. In the blink of an eye, Acme realizes that by changing suppliers, it will lose the contingent workforce it has trained and used for years.

Are noncompete agreements preventing temps from remaining on the job when their employer loses the contract enforceable? More than 20 years ago, *Consultants & Designers, Inc. v. Butler Serv. Group, Inc.*,¹ first announced that such noncompetes do protect a reasonable business interest. Since then, other courts, using a more traditional analysis, have refused to enforce noncompetes against temporary employees.²

Use of noncompete agreements between staffing companies³ and their assigned employees⁴ is controversial, and on the rise. These agreements are generally unknown to the customer. Customers learn of them when they switch vendors, when they reduce their vendor base, or when they choose other business strategies, such as outsourcing the operation. Sometimes injunctions are sought against employees who seek to join the incoming firm. More often, the outgoing firm sues the incoming vendor for tortious interference with the noncompetes, squandering the competitor's profits in defense of the claims.

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1. 720 F.2d 1553 (11th Cir. 1983).

2. See, e.g., *Nat'l Employment Serv. Corp. v. Olsten Staffing Serv.*, 761 A.2d 401, 405 (N.H. 2000).

3. Various known as professional employer organizations (PEOs), contract houses, temporary agencies, or employee leasing companies.

4. Referred to as contractors, "temps," contingent workers, or leased staff.

II. The Protectable Interest

Generally, noncompetes are enforceable only if they protect an “employer’s reasonable competitive business interests.”⁵ Courts commonly require a “showing that enforcement of a covenant is reasonably *necessary*” to the company’s business.⁶ A restraint greater than needed is simply unreasonable and unenforceable.⁷ Historically, the employer must demonstrate that the restrained employee either has access to confidential information or has contact with and influence over customer decision makers, so as to be able to affect the employer’s customer goodwill. In the staffing industry, for example, account managers in charge of the customer relationship and recruiters with access to the staffing firm’s database of candidates and job openings are clearly subject to restraint.⁸

Under traditional analysis, a temporary help company would have no hope of enforcing a noncompete against a contracted employee after it lost the contract. Though these employees may (or may not) know the person who decides which vendor gets the contract, they have no sway over her or him.⁹ For example in *Hasty v. Rent-a-Driver*,

5. *Arthur Murray Dance Studios v. Witter*, 105 N.E.2d 685, 694–95 (Ohio Misc. 1952); *Hapney v. Cent. Garage Inc.*, 579 So. 2d 127, 130 (Fla. Dist. Ct. App. 1991) (The “overwhelming majority” of states that permit employee noncompete agreements require “at a minimum that such contracts be reasonably related to the protection of a ‘legitimate business interest’ or ‘protectable interest’ of the employer.”); *Patio Enclosures, Inc. v. Herbst*, 39 Fed. Appx. 964, 967–68, 2002 U.S. App. LEXIS 14017 (6th Cir. 2002); *Labor Ready Inc. v. Abis*, 767 A.2d 936, 942 (Md. Ct. Spec. App. 2001); *Gateway 2000, Inc. v. Kelley*, 9 F. Supp. 2d 790, 795 (E.D. Mich. 1998); *Kadco Contract Design Corp. v. Kelly Servs., Inc.*, 38 F. Supp. 2d 489, 496 (S.D. Tex. 1998).

6. *Follmer, Rudzewicz, & Co. v. Kosco*, 362 N.W.2d 676, 683 n.18 (Mich. 1984), *Arthur Murray Dance Studios*, 105 N.E.2d at 694–95; *Gateway 2000*, 9 F. Supp. 2d at 795; *Herbst*, 39 Fed. Appx. at 967–68.

7. RESTATEMENT (SECOND) OF CONTRACTS §188(2)(b)(1989); *Herbst*, 39 Fed. Appx. at 970; *Kelsey-Hayes Co. v. Maleki*, 765 F. Supp. 402, 406, (E.D. Mich. 1991), *vacated by settlement* 889 F. Supp. 1583 (E.D. Mich. 2001).

8. *Robert Half Int’l v. Van Steenis*, 784 F. Supp. 1263, 1274 (E.D. Mich. 1991); *Courtesy Temp. Serv., Inc. v. Camacho*, 272 Cal. Rptr. 352, 357, 361 (Cal. Ct. App. 1990); *Hapney*, 579 So. 2d at 130 (“The rule, generally stated, is that an employer may not enforce a post-employment restriction . . . simply to eliminate competition per se; the employer must establish its legitimate business interest to be protected.”).

9. Mere contact with a customer is insufficient without the ability to influence the decision. *See Standard Register Co. v. Cleaver*, 30 F. Supp. 2d 1084, 1097 (N.D. Ind. 1998). “[T]he mere opportunity of the employee to become acquainted with a customer does not determine the need . . . of the protection, rather the personal relationship . . . must be taken into account so as to indicate the likelihood that the employee would be able to take the customers of his employer when he leaves.” *Id.* at 1097. The seminal *Arthur Murray Dance Studios* refers to the “much abused, much-misunderstood and much-misapplied” customer-contact theory: “Mere customer contact and nothing more doesn’t always bring the customer so completely under his spell that the customer will automatically move with the employee wherever the employer goes.” *Arthur Murray Dance Studios*, 105 N.E.2d at 705. *Blake* similarly observes: “The mere fact of frequent customer contact is not enough to provide a basis for an enforceable covenant when the circumstances of the contact are such that the risk to the employer is low . . . such as is often the case with office workers, clerks in retail stores, auto mechanics, repairmen and the

Inc.,¹⁰ the court negated the covenant of a leased truck driver who went to a competitor serving the same customer, because he had no influence on the customer's decision to use his employer or the competitor.¹¹ Similarly, in *Nat'l. Employment Serv. Corp. v. Olsten Staffing Serv., Inc.*,¹² the court noted that the temporary employees "were not in a position to appropriate the company's goodwill and were without access to sensitive information."¹³ Notably, while temps may work with the customer's confidential information, they seldom know the staffing company's secrets, which are generally limited to its margin, or its database of prospective employees.

The fact that the outgoing firm has generally already lost the contract before employees seek to migrate to an incoming company demonstrates that the "temps" have no effect on goodwill. *Ramsey v. Guardsmark, Inc.*,¹⁴ notes this lack of causation, while resurrecting the employee's tortious interference claims against his or her former employer for using unreasonable noncompetes to squelch prospective employment with an incoming company.¹⁵ The *Guardsmark* court stated the staffing company's "business interest" was "severely diminished" because the contract had already been lost when it sought to enforce the noncompete, and had no other jobs for the employees.¹⁶ *Volt Services Group v. VIA Management Tools, Inc.*,¹⁷ likewise touches on this concept, en route to dismissing tortious interference claims against the incoming company.¹⁸ Noting that an arbitrator in an underlying proceeding had found that the outgoing firm "never submitted a bid" to remain on-site as a managed service provider, and that the employees' migration did not cause the loss of the employer's business, the federal court gave collateral estoppel effect to the arbitrator's declaration that the outgoing firm's noncompetes were "not enforceable . . . and . . . not designed to protect reasonable business interests."¹⁹

Employers may not use noncompete agreements to merely corral their employees.²⁰ Noncompetition clauses in employment contracts

like." Harlan Blake, *Employment Agreements Not to Compete*, 73 HARV. L. REV. 625, 663 (1960).

10. 671 S.W.2d 471, 473 (Tenn. 1984).

11. *Id.* at 494.

12. 761 A.2d 401, 405 (N.H. 2000).

13. *Id.* at 405.

14. 1994 U.S. App LEXIS 13457 (10th Cir. 1994).

15. *Id.* at 6-7.

16. *Id.*

17. 2003 U.S. Dist. Ct. LEXIS 20942 (E.D. Mich. 2003).

18. 2003 U.S. Dist. Ct. LEXIS 20942 at *3-4.

19. *Kadco Contract Design Corp.*, 38 F. Supp. 2d at 489. This case likewise declares a noncompete against temporary employees unenforceable, stating that "the covenant was not ancillary to an otherwise enforceable agreement." *Id.*

20. "The essential purpose of the post employment restraint . . . is not to prevent the competitive use of the unique personal qualities of the employee—either during or after employment—but to prevent competitive use, for a time, of information or relation-

have been the source of litigation for over 500 years.²¹ Keeping an employee's talents from competitors is universally rejected as a sufficient interest to support a noncompete.²² Actually, the exact opposite is true: the employer must "persuade the court that the motivating reason for the covenant is *not* to establish a hold upon the employee."²³ The court in *Labor Ready Inc. v. Abis* stated:

The essential purpose of the post-employment restraint . . . is not to prevent the competitive use of the unique personal qualities of the employee—either during or after the relationship—but to prevent competitive use, for a time, of information or relationships which pertain peculiarly to the employer and which the employee acquired in the course of employment.²⁴

All employers compete to attract and retain employees. Noncompete agreements, which limit this competition, are in restraint of trade.²⁵ Thus, to be sustained as reasonable, the employer's "interest [protected by a non-compete] must be something greater than mere competition, because prohibition of competition is in restraint of trade."²⁶

The Federal Trade Commission has observed that temporary help companies compete by hiring employees of other temporary help firms.²⁷ In the *Matter of National Assoc. of Temporary Services, Inc.*, the FTC restrained a trade organization, which is now the American Staffing

ships which pertain to the employer and which the employee acquired in the course of the employment." Blake, *supra* note 9, at 647; *Arthur Murray Dance Studios*, 105 N.E.2d at 695 ("Is the real object just to prevent the employee from quitting . . . ?" "Is the real object merely to remove a competitor and ordinary competition?"); *Hapney*, 579 So. 2d at 130.

21. *Ram Prod. Inc. v. Chauncey*, 967 F. Supp. 1071, 1091 (N.D. Ind. 1997) (citing Blake, *supra* note 9 (citing *Mitchell v. Reynolds*, 1 P. Wms. 181, 24 Eng. Rep. 347 (Q.B., 1711))). *Mitchell* is based upon earlier cases striking down restraints where craftsmen sought to prolong the subservience of apprentices in violation of guild custom. See *generally Mitchell*, 24 Eng. Rep. at 347.

22. Arguments that, after training an employee, an employer should be permitted to restrain the employee from going into competitive employment "have not proven sufficiently persuasive. It has been *uniformly held* that general knowledge, skill, or facility acquired through training or experience while working for an employer appertain exclusively to the employee." Blake, *supra* note 9, at 652 (emphasis added). "[T]he employer should be in a position to persuade a court that the motivating reason for the covenant is not to establish a hold upon the employee . . . but to protect legitimate business interests . . ." See *supra* notes 18, 20.

23. Blake, *supra* note 9, at 687.

24. *Labor Ready Inc. v. Abis*, 767 A.2d 936, 943 (2001).

25. *Volt Serv. Group v. Adecco Employment Servs., Inc.*, 35 P.3d 329 (Or. Ct. App. 2001). See also *Kadco Contract Design Corp.*, 38 F. Supp. 2d at 495. This case likewise declares a noncompete against temporary employees unenforceable, stating that the covenant was not ancillary to an otherwise enforceable agreement." *Id.*

26. *Chauncey*, 967 F. Supp. at 1091–92; *United Rentals v. Keizer*, 202 F. Supp. 2d 727, 740 (W.D. Mich. 2002), *Kelsey-Hayes Co.*, 765 F. Supp. at 407, *vacated by settlement*, 889 F. Supp. 1583 (E.D. Mich. 2001).

27. In the *Matter of Nat'l Assoc. of Temp. Servs., Inc.*, 106 F.T.C. 545 (1985) (a proceeding regarding efforts to restrain the movement of temporary employees from one member company to another).

Association, from maintaining a code of ethics that prevented members from recruiting or employing temporary help employees registered with competitors.²⁸

III. The Disintermediation “Interest”

After centuries of noncompete litigation, an aberration occurred in *Consultants & Designers, Inc. v. Butler Serv. Group, Inc.*²⁹ Completely without citation to precedent, the court simply invented a new protectable interest for the staffing industry, based upon the astonishing premise that a corporation has a “property interest in its” employees.³⁰ *Volt Services Group v Adecco Employment Serv., Inc.*, followed *Consultants*, holding that temporary employees were the “commodity” of the employer.³¹

Consultants states that “some form of contractual constraint” is necessary to protect the staffing company’s “role as . . . the much maligned but time-honored middleman,” whose function is to “gather . . . and to provide information on available and suitable people for” the customer.³² The alleged and admittedly “only possible” justification for a covenant restraining temps is to prevent a customer from cutting out the middleman, a process known as “disintermediation.”³³

Thus, *Consultants* simply announced a new protectable interest to sustain the staffing industry while literally relegating the employees to the status of the company’s property. Remarkably, *Consultants* created this new interest in text covering two and a half pages without citing a single case from the past 500 years. If only the court had sought to anchor its rationale in precedent, it would have seen that its rationale stands in contrast to long-standing principles. Virtually every premise of the opinion is demonstrably incorrect.

IV. The Fundamental Premise that Outgoing Staffing Firms Must Keep Temporary Employees from Incoming Firms has been Rejected by the Staffing Industry

Reversing a half-millennium of precedent, *Consultants* and *Volt v. Adecco* enforce noncompetes that protect no interest except to keep employees from the plaintiff’s competitors. Which company would not im-

28. *Id.*

29. See generally *Consultants & Designers, Inc. v. Butler Serv. Group, Inc.*, 720 F.2d 1553 (11th Cir. 1983).

30. *Id.* at 1559.

31. *Volt Serv. Group*, 35 P.3d at 333 (Because this 2001 Oregon case involves the same plaintiff as the 2003 decision in *Volt Serv. Group v. VIA Management Tools, Inc.*, 2003 U.S. Dist. Ct. LEXIS 20942 (E.D. Mich. 2003), the decisions will be referred to as *Volt v Adecco* and *Volt v. VIA* for clarity.)

32. *Consultants & Designers, Inc.*, 720 F.2d at 1558.

33. *Id.*

prove its competitive posture if it could prevent talented employees from taking positions with competitors?³⁴ They don't, because they can't.

Not only has *Consultants* ignored this basic point, but the decision's foundational premise that staffing companies need protection from the loss of employees to incoming firms has been rejected by the dominant trade group in the staffing industry.

The American Staffing Association (ASA) represents 1,500 members, including 85 percent of the staffing industry by sales volume.³⁵ Without question, it is the dominant industry association. The ASA has published a code of ethics that says when another company has obtained the contract to provide staff, the temporary employees should be given "the choice of . . . applying to stay on their current assignment with the new staffing firm" or serving other customers of the outgoing firm.³⁶

Contrary to the assumption inherent in *Consultants* that staffing firms need protection from disintermediation, the ASA has decreed that allowing temps to migrate from outgoing firms to incoming firms is "in the best interests of the staffing industry."³⁷ How can noncompete

34. No court would ever find that a construction crane operator could be constrained with a noncompete agreement merely on the basis of his or her talents. Yet, a company employing most of the few skilled crane operators in a city could disarm potential competitors and retain their business by locking the crane operators up with a noncompete agreement.

35. The American Staffing Association, Staffing FAQs at <http://www.staffingtoday.net/staffstats/staffingfaqs.html>.

36. *Id.* Industry customers and guidelines are relevant when scrutinizing a party's attempt to restrain competition by employees. The "most cited" case on common-law restraints in 250 years, *Mitchell v. Reynolds*, is based upon four earlier cases striking down restraints where craftsmen sought to prolong the subservience of apprentices "in violation of guild custom." Blake, *supra* note 9, at 629, 632.

37. The American Staffing Association Code of Ethics states in relevant part as follows:

As a condition of membership in the American Staffing Association, each member pledges its support of, and adherence to the principle set forth below. Through their voluntary compliance with these principles, ASA members acknowledge that such compliance is in their best interest of the staffing services industry . . . ASA members agree to always strive:

* * *

To observe the following guidelines to ensure an orderly transition when taking over an account being serviced by another staffing firm:

The outgoing firm should, whenever feasible, be given reasonable prior notice that the account is being transferred;

Assigned employees of the outgoing firm should, whenever feasible, be allowed to continue working on the payroll of the outgoing firm for some reasonable transition period; thereafter, they should be given the choice of accepting an assignment with another customer of an outgoing firm or applying to stay on their current assignment with the new staffing firm.

The American Staffing Association, *supra* note 35.

Interestingly, in October, 2003, the ASA modified its code of ethics to state: "These guidelines are subject to enforceable contracts between staffing firms

agreements for temps be “reasonably necessary” to protect staffing companies when the dominant trade group states that the temporary employees of its members must be allowed to apply to incoming firms as a matter of ethics?

The discussion of the ASA code of ethics cannot end without stating the obvious corollaries: If it is in the best interests of the staffing industry to allow temps to migrate to incoming firms, then handcuffing temps must be contrary to the staffing industry’s interests. Of course it is. Clearly, if it became commonly known that customers of temporary services could be stripped of their workforce if the relationship with the vendor ends because of secret noncompete agreements, most corporate customers would avoid the staffing industry option for other business models, such as outsourcing.

Another necessary corollary: If, as a matter of ethics, the temporary employees should be given the chance to apply to incoming firms, why isn’t it “unethical” to bind them to noncompete agreements that prevent them from doing so. Who wouldn’t agree that it is unethical for a Fortune 500 staffing company to make the temporary employees its pawns in any dispute with the corporate customer and incoming vendor? Yet, many of the above-cited decisions show that outgoing staffing firms sue incoming companies with the temps caught in the middle. Thus, not surprisingly, the ASA code of ethics recommends that this issue be addressed in negotiations between the corporate entities with equal bargaining power. It states: “ASA members are encouraged, whenever feasible, to specifically address the terms and conditions relating to the transfer of accounts in written agreements *with their customers*.”³⁸ (emphasis added.)

V. No Human Being Has Been the “Commodity” of Any Employer Since the Emancipation Proclamation

Foundational to both *Consultants* and *Volt v. Adecco* is the premise that the employer has a “property interest” in the employee. *Volt* goes so far as to say that temps are the “commodity” of the staffing firm.³⁹ Fortunately, the belief that an employer can have a property interest in a human being has been out of favor since the Emancipation Proclamation. A court decision declaring a property interest in human be-

and their customers, employees, and other parties . . .” The American Staffing Association, *supra* note 35. However, the modification of the code of ethics does not undercut the rationale: If the general rule is that employees should be able to apply to incoming companies as a matter of ethics, why is it “necessary” for some ASA member firms to use noncompetes to restrain employees? *Id.*

38. The American Staffing Association, *supra* note 35.

39. *Volt*, 35 P.3d at 334. “[W]orkers are *the very commodity* in which both the plaintiff and defendant deal.” *Id.*

ings is repugnant to the Thirteenth Amendment to the U.S. Constitution, which outlawed involuntary servitude within the United States.⁴⁰

Discussing the Thirteenth Amendment, the Supreme Court in *Pollack v. Williams*,⁴¹ stated:

The undoubted aim of the Thirteenth Amendment . . . *was not merely to end slavery but to maintain a system of completely free and voluntary labor* throughout the United States . . . [I]n general the defense against oppressive hours, pay, working conditions, or treatment is *the right to change employers*.⁴²

Other noncompete cases and commentators recognize that an employer has no property interest in a worker. On the contrary, the law is uniform that the employee “owns” his skills: “A man’s aptitudes, his skill, his dexterity, his manual and mental ability . . . *they are not his master’s property; they are himself*.”^{43, 44}

When pressed, staffing companies asserting noncompetes sometimes retreat and claim the “property interest” protected is actually the contractual right contained in the agreement. Certainly, it is theoretically possible to have property interests in contractual rights.⁴⁵ However, unless one is dizzied by circular logic, the flaw in this argument should be apparent:

Noncompete agreements are not enforceable unless they protect some reasonable interest of the employer beyond the mere restraint of employees;

Under *Consultants*, the reasonable business “interest” allegedly protected is the employer’s property interest in the Noncompete agreement.

The Agreement restrains the employee from working for a competitor.

Thus, the supposed interest of the employer is to keep the employee from competitors.

40. Previously, when noncompete cases discussed the application of the Thirteenth Amendment, it was to note that although the Constitution prevented specific enforcement of a personal services contract, a court could enjoin one from performing for another. *Managed Health Care Assocs., Inc. v. MHCA Acquisition, Inc.*, 209 F.3d 923, 929–30 (6th Cir. 2000). However, no case has yet discussed the notion that a corporation may restrain an employee because the employee is the commodity of the corporation.

41. *Pollack v. Williams*, 322 U.S. 4 (1944).

42. *Id.* at 17.

43. *Hill v. Mobile Auto Trim*, 725 S.W.2d 168, 172 (1987) (quoting Williston on Contracts § 1646) (emphasis added).

44. *See also* *Thomas v. Best Mfg. Corp.*, 218 S.E.2d 68, 70 (Ga. 1975) (Noncompete agreement void and contrary to law, except where it protects trade secrets, because “a man’s aptitude, his skill, his dexterity, his manual and mental ability, and such other subjective knowledge as he obtains while in the course of his employment, are not the property of his employer.”) (internal quotations omitted).

45. *Bd. of Regents of State of Colleges v. Roth*, 408 U.S. 564, 577 (1972). This case stands for that proposition, and also notes that there is no property interest where the employment is “at-will.” *Id.*

For centuries, the desire to keep talent from competitors did not justify noncompete agreements. But *Consultants* creates an exception for staffing companies. Showing that the analogy to antebellum slavery is not as fanciful as one might think, *Consultants* observes that the employer could have “sold” its “property interest in the job shoppers.”⁴⁶

This statement demonstrates that *Consultants* misses a basic point of noncompete law. Restrictive covenants are only reasonable, and thus sustainable despite their restraint on trade, because the employer would suffer irreparable harm if the employee, and thus the employer’s confidential information or the one responsible for its customer relationship, gets into the hands of a competitor.⁴⁷ The suggestion that the employees may go to a competitor without causing damage, as long as bounty, booty or tribute is paid by the hiring employer, demonstrates that no legitimate interests exist. The only interest protected is the restraint itself, which can be relinquished for a price, with no resulting harm to the employer.

Which employer would not want to be in the position of holding its employees for ransom, so that they may not migrate to a competitor? Why is this rationale confined to the staffing industry? Why shouldn’t any company losing a project or customer be able to charge incoming competitors for hiring its employees as they follow the work? They don’t because they can’t.

VI. The Employee Has a Superior “Property” Right to Information About Himself

It is black letter noncompete law that “knowledge, skill, or facility gained through . . . experience while working for an employer appertain[s] exclusively to the employee,” and is not “a sufficient interest to support a restraining covenant”⁴⁸ If one’s skills and talents are one’s own, then how does *information about* one’s skills and talents come to be the employer’s exclusive property so that the employee cannot use it to market himself? But *Consultants* deems this so.

Consultants essentially holds that the employer may restrain a temporary employee because the employer learned of the employee’s skills and passed that information on to its customer.⁴⁹ Does a staffing

46. *Consultants & Designers Inc.*, 720 F.2d at 1559.

47. The vast majority of noncompete cases involve request for injunctive relief because of the “irreparable harm” that would result to the former employer if the employee were to work for a competitor. Thus, some statutes proved that reasonable noncompete agreements are specifically enforceable. See, e.g., MICH. COMP. LAWS § 445.774a (2005).

48. *Follmer, Rudzewicz, & Co.*, 362 N.W.2d at 681 n.4 (1984), quoting Blake, *supra* note 9, at 652; *Chauncey*, 967 F. Supp. at 1088; *Thomas*, 218 S.E.2d at 788–89; *Hill*, 725 S.W.2d at 172.

49. *Consultants & Designers Inc.*, 720 F.2d at 1558. “Whatever ancillary services Butler supplied to [the customer], it was as a provider of information that Butler performed its essential function. Butler’s role was to gather, distill, and provide to [the customer] information on available and suitable people. . . .” *Id.* Other courts recognize this

employer gain control of the employee's future ability to market herself merely because the employer found the employee's resume on Monster.com? Is this not plainly less justification for a covenant than that rejected in a myriad of cases—that the employer trained the employee? But knowledge and skills gained during employment do not justify non-competes.⁵⁰

Consultants does more violence to longstanding principles of non-compete law than is immediately apparent. *Consultants* actually grants staffing companies the right to restrain employees because of “knowledge, skill or facility” gained in *past employment* that the employee reports to the staffing company in the application process.⁵¹ Even conceding that a staffing company can keep data about its bank of prospects from being used by recruiters who leave, does not the employee have a superior interest to use information about his own skills to market himself, especially when those skills were honed before the staffing company found him?

Moreover, while information about the employee may have been “confidential” at some point, confidentiality is no justification to restrain employees after the contract is lost.⁵² Information is no longer confidential to the staffing company once the employee began performing in the customers' environment, and the employee's skills and talents became known to the customer and other staffing firms on site.⁵³ Outside the staffing industry, courts scrutinize claims of confidentiality,

does not constitute a protectable interest. See *Ramsey v. Guardsmark*, 1994 U.S. App. LEXIS 13457, at *6 (10th Cir. 1994) (unpublished opinion) (holding that the outgoing employer had no reasonable interest in the restraint of temps after it had lost the contract, even though it had “commit[ed] substantial resources to recruitment”).

50. The states of Florida and Kentucky are in the minority and have held that specialized training can be a protectable interest. See *Aero Kool Corp v. Ooshuizen*, 736 So. 2d 25 (Fla. Dist. Ct. App. 1999); *Balasco v. Gulf Auto Holding, Inc.*, 707 So. 2d 858, 860 (Fla. Dist. Ct. App. 1998) (notable for its statement that noncompete was necessary to protect against the loss of “experienced” employees because that has a negative effect of “productivity,” without recognizing that the noncompetes merely restrained trade for the economic benefit of the employer); *Cent. Adjustment Bureau v. Ingram Assocs., Inc.*, 622 S.W.2d 681, 686 (Ky. Ct. App. 1981) (but noting that after receiving specialized training, the employees could pirate away the employer's customers, thus linking training to a good-will interest).

51. *Consultants & Designers Inc.*, 720 F.2d at 1558. Here the court stated:

Butler's role was to gather, distill, and provide to TVA information on available and suitable people for TVA's positions . . . If Butler's covenant with its job shoppers is to have any justification, that justification must be to protect Butler's role as middleman in the market for information . . .

Id.

52. See *Guardsmark*, 1994 U.S. App. LEXIS 13457, at *7–8 (where the employer has lost the contract and cannot place the employee with another customer, the employer's interest is “severely diminished”).

53. See *Consultants & Designers Inc.*, 720 F.2d at 1558 (acknowledging that once the employer has connected the employer and the customer, its “primary mission” is complete).

and consistently refused to enforce noncompetes when the information is not confidential at all.⁵⁴ In contrast, *Consultants* gives the entire staffing industry a free pass on the issue of confidentiality.

VII. Can An Employer Assert a Noncompete Because It Recruited the Employee?

What employer wouldn't love to be able to justify a noncompete because it recruited the employee? If that were justification for a noncompete, virtually every employer would be in a position to keep all of their employees from competitors, even if they had no effect on customer relations or contact with confidential information. If recruiting efforts sufficed, why have courts bothered to examine the employer's other interests in enforcing the noncompete?

The outgoing staffing firm in *Nat'l Employment Serv. Corp. v. Olsten Staffing Serv. Inc.*,⁵⁵ attempted to argue that its hiring efforts and expertise justified a noncompete to retain employees for a sufficient period to recoup costs associated with recruiting, interviewing, qualifying and placing its employees.⁵⁶ But employers have been gathering, distilling, and providing information on available and suitable people for centuries. The court reigned in this argument:

*All businesses, however, incur expenses in recruiting and hiring employees. National does not allege that the restrictive covenant was necessary to prevent its employees from appropriating the company's confidential information, trade secrets, or goodwill . . . Post-employment restrictions on such employees would be contrary to public policy . . .*⁵⁷

Consultants ignored this reality when it sustained the covenant, noting, "Butler's role was to gather, distill and provide . . . information on available and suitable people."⁵⁸ The difference between *Olsten* and *Consultants* can be explained by the fact that the New Hampshire Supreme Court analyzed this novel argument under traditional noncompete law, while *Consultants* shot from the hip, without precedent.

If the staffing company's importance to the customer is its ability to find talented employees, then customers have merely outsourced the

54. *Kelsey Hayes Co.*, 765 F. Supp. at 407; *Gaynor & Co. v. Stevens*, 61 A.D.2d 775, (N.Y. App. Div. 1978) (where customer's identity is readily ascertainable from outside sources, "solicitation [of customers] by the employees will not be enjoined"); *Jostens, Inc. v. Nat'l Computer Sys., Inc.*, 318 N.W.2d 691, 702 (Minn. 1982) (action against employees for misappropriation of trade secrets in the form of custom configuration of its commercially purchased computer system failed, because the employer took no effort to preserve secrecy).

55. See generally *Nat'l Employment Serv. Corp. v. Olsten Staffing Serv. Inc.*, 761 A.2d 401 (N.H. 2000).

56. *Id.* at 405.

57. *Id.* (emphasis added).

58. *Consultants & Designers Inc.*, 720 F.2d at 1558.

recruiting and hiring functions that have traditionally been performed in-house to staffing firms.⁵⁹ The staffing industry has chosen to occupy a niche performing hiring functions that historically have not supported a noncompete. There is no reason to trump employees' longstanding right to apply to companies that have work to offer. If Ford Motor Company can't prevent laid-off die makers from going to GM because GM is selling more cars and thus has jobs available, why should the plaintiffs in *Consultants* or *Volt* be able to hold their employees when they lose a staffing contract?

VIII. A Better Solution: Transition Provisions in Contracts with the Customer

Apparently without recognizing the import of its words, *Consultants* notes that enforcement of a noncompete is not the only way or even the best way to protect staffing companies.⁶⁰ However, a covenant must be "reasonably necessary" to protect the employer's interests.⁶¹ Moreover, in other contexts, most noncompete litigation seeks an injunction because of the irreparable harm that would occur if the employee became employed by a competitor.⁶² That harm would be irreparable demonstrates that the covenant is necessary. In contrast, suits by staffing firms often do not seek an injunction.⁶³ Rather, they seek damages for breach of contract or tortious interference with the noncompete. However, the unspoken corollary is that if there is not irreparable harm, neither is there a protectable interest. Where, as *Consultants* concedes, there is another way to protect the employer's interests, noncompetes are not reasonably necessary.

The "other way" to avoid the proclaimed danger of "disintermediation" conceded by the court in *Consultants* is the method recommended by the American Staffing Association code of ethics, as quoted above: "ASA members are encouraged, whenever feasible, to specifically address the terms and conditions relating to the transfer of accounts in written agreements with their customers."⁶⁴

Indeed, case law supports "conversion fees" where the temporary employee is hired away from the staffing firm.⁶⁵ This is apparent in *Adia Serv., Inc. v. Sansone*,⁶⁶ as well as *Aerotek v. Burton*.⁶⁷

59. That is signified by the moniker "Professional Employer Organization."

60. *Consultants & Designers Inc.*, 720 F.2d at 1560.

61. See *supra* note 4.

62. The overwhelming majority of cases cited herein seek injunctive relief. See *supra* notes 4, 9, 21.

63. *Volt*, 35 P.3d at 333; *Nat'l Employment Serv. Corp.*, 761 A.2d at 405.

64. The American Staffing Association, *supra* note 35 (emphasis added.).

65. *Adia Serv., Inc. v. Sansone*, 793 S.W.2d 643, 644 (Mo. App. 1990).

66. *Id.*

67. *Aerotek v. Burton*, 835 So.2d 197, 201 (Civ. App. Ala. 2001). This, while recog-

The primary problem for staffing companies is that by seeking to negotiate a transition fee, some customers will reject their proposal in favor of companies that do not require transition arrangements. Other customers will negotiate transition provisions that reasonably relate to the staffing company's interests. Typically, such provisions involve a sliding scale depending upon the length of time that the employee has been on the assignment (and thus depending on the profits already realized).

IX. Conclusion

The law's usual hostility to restraints upon a worker's right to advance his or her career has been strangely relaxed with regard to temporary workers, who are possibly more vulnerable than "regular" employees. The 1983 *Consultants* opinion, decided when the staffing industry was in its infancy, granted a "protectable interest" to restrain temporary workers without analysis of the preceding half millennium of noncompete law. Now, a case from the new millennium has breathed new life into the "disintermediation" interest. However, other courts, employing traditional analysis, recognize that temporary employees implicate virtually none of the interests that have traditionally justified noncompete agreements.

nizing the "disintermediation" interest over a dissent that finds no protectable interest, required the employee to pay a conversion fee if he were to take employment directly or indirectly with the customer. *Id.*