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Supreme Court Roundup: The High Court's Significant Labor and Employment Law Decisions of the 2004-05 Term

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Introduction

The Supreme Court's 2004-05 term produced significantly fewer employment law decisions than in recent terms. Nevertheless, the Court resolved a few circuit splits and opened the door for new types of claims under anti-discrimination statutes, only one of which affects private employers. This article will outline three of the Court's most significant employment law opinions from the recent term. In addition, this article will highlight two employment law cases on the Supreme Court's docket as part of the 2005-06 term.

Supreme Court's Significant Employment Decisions in the 2004-05 Term

ADEA Allows Disparate Impact Claims

Smith v. City of Jackson, 125 S.Ct. 1536 (decided March 30, 2005)

In *Smith v. City of Jackson*, 125 S.Ct. 1536 (2005), the Supreme Court recognized that the Age Discrimination in Employment Act of 1967, as amended, 29 U.S.C. § 621, *et seq.* ("ADEA"), authorizes recovery in disparate-impact cases.

In *Smith*, police and safety officers in Jackson, Mississippi brought claims against the City of Jackson (the "City") under the ADEA, which prohibits discrimination in employment on the basis of age with respect to individuals who are 40 years of age or older. The officers alleged that they had received less generous salary increases than those received by younger officers. The City's salary increase plan, implemented on October 1, 1998, was designed to "attract and retain qualified people, provide incentive for performance, maintain competitiveness with other public sector agencies and ensure equitable compensation to all employees regardless of age, sex, race and/or disability." *Smith*, 125 S. Ct at 1539. As a result of this plan, those officers with less than five years of tenure received proportionately greater salary increases compared to their former pay than those with more seniority. While some officers over 40 had less than five years of service, most of the officers over 40 had been employed by the City more than five years. The older officers claimed that the City deliberately discriminated against them on the basis of their age (the disparate-treatment claim) and that they were "adversely affected" by the plan because of their age (the disparate-impact claim).

The District Court granted summary judgment for the City, and the Court of Appeals for the Fifth Circuit affirmed, finding that disparate-impact claims are categorically unavailable under the ADEA. In dicta,

the Fifth Circuit assumed that the facts alleged by the officers would allow them to seek relief under *Griggs v. Duke Power Co.*, 401 U.S. 424 (1971), which established a disparate-impact theory of recovery under Title VII of the Civil Rights Act of 1964 ("Title VII").

In a 5-3 decision, the Supreme Court affirmed the judgment of the Fifth Circuit, but on different grounds. It recognized that the ADEA authorizes recovery for disparate-impact claims in cases comparable to *Griggs*. Writing for the majority, Justice John Paul Stevens noted that neither Title VII "nor comparable language in the ADEA simply prohibits actions that 'limit, segregate, or classify' persons; rather the language prohibits such actions that 'deprive any individual of employment opportunities or *otherwise adversely affect* his status as an employee, because of such individual's' race or age." *Smith*, 125 S.Ct. at 1542 (quoting 42 U.S.C. § 2000e-2(a)(2)[Title VII])(emphasis in original). Statutory language in both the ADEA and Title VII "focuses on the *effects* of the action on the employee rather than the motivation for the action of the employer." *Id.* The Court also recognized that despite the virtually identical clauses in these two statutes, the ADEA's coverage for a disparate-impact claim is more limited than that of Title VII in that the ADEA permits any "otherwise prohibited" action "where the differentiation is based on reasonable factors other than age." § 4(f)(1) of the ADEA. The Court determined that Congress' choice to limit the ADEA's coverage by including the "reasonable factors other than age" ("RFOA") provision is consistent with the fact that age, unlike Title VII's protected categories (race, color religion, sex, or national origin), generally has relevance to an individual's ability to engage in certain types of employment.

While the Court's recognition of a disparate-impact ADEA claim appears favorable for the officers in *Smith*, their claim failed on its merits because they were unable to isolate and identify "the specific employment practices that are allegedly responsible for any observed statistical disparities." *Smith*, 125 S.Ct at 1545. Instead, the Court noted that the employees "did little more than point out that the pay plan at issue is relatively less generous to older workers than to younger workers. They [did] not identif[y] any specific test, requirement, or practice within the pay plan that has an adverse impact on older workers." *Id.* The Court found that the City's criteria of using seniority and rank is "unquestionably reasonable" considering the City's "goal of raising employees' salaries to match those in surrounding communities." *Id.* at 1546. Accordingly, the City's choice was based on "a reasonable factor other than age." Even though there could have been other reasonable ways that did not have a disparate impact on older workers, the reasonableness inquiry, "[u]nlike 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, … includes no such requirement." *Id.*

The Court's ruling *Smith v. City of Jackson* will likely generate more disparate-impact claims from older employees. Such claims, unlike disparate-treatment claims, do not require a showing of discriminatory intent. Instead, they center on whether an employer's policies and practices adversely affect a protected group. The Court's previous decision in *Hazen Paper v. Biggins*, 507 U.S. 604 (1993), prompted several circuit courts, including the Third Circuit, to conclude that the ADEA did not authorize a disparate-impact theory of liability.[1]

[1] In *Hazen*, the Court held that an employee's allegation that he was discharged shortly before his pension would have vested did not state a cause of action under a disparate-treatment theory on the ground that the employer's motivating factor was not the employee's age but his years of service, which is not a protected characteristic under the ADEA.

In light of *Smith*, employers should review their benefit and compensation packages to determine if there is an adverse impact on older workers or any other protected group. Because employees can now establish a prima facie case by pointing to compelling statistical disparities, employers should proactively perform statistical analysis to identify and correct any potential disparate impact on older workers resulting from an employer's practice or policy.

The Supreme Court Allows a Title IX Private Right of Action for Retaliation

Jackson v. Birmingham Board of Education, 125 S.Ct. 1497 (decided March 29, 2005)

In *Jackson v. Birmingham Board of Education*, 125 S.Ct. 1497 (2005), the Supreme Court expanded the scope of Title IX of the Education Amendments of 1972, 20 U.S.C. §§ 1681, *et seq.* ("Title IX"), by finding that a male coach who complained about discrimination against his girls' basketball team could sue for retaliation despite the fact that retaliation is not mentioned in Title IX, which prohibits sex discrimination by recipients of federal education funding.

In *Jackson*, a former coach of a girls' high school basketball team discovered that his team was not receiving equal funding and equal access to athletic facilities and equipment and complained to his supervisors. He then received negative work evaluations and was ultimately removed as the girls' basketball coach and no longer received supplemental pay for coaching. The coach brought a claim against the board of education alleging that it retaliated against him in violation of Title IX because he had complained about alleged sex discrimination in the school's athletic program.

The United States District Court for the Northern District of Alabama dismissed the complaint on the ground that Title IX's private cause of action does not include claims of retaliation, and the Eleventh Circuit affirmed. 308 F.2d 1333 (11th Cir. 2002). The Eleventh Circuit also noted that even if Title IX does allow a claim for retaliation, the coach is not within the class of persons the statute protects.

In a narrow 5-4 decision, the Supreme Court held that "Title IX's private right of action encompasses suits for retaliation, because retaliation falls within the statute's prohibition of intentional discrimination on the basis of sex." *Jackson*, 125 S.Ct. at 1507. It also recognized that the coach could assert a retaliation claim even though he was not a victim of the discrimination that was the subject of his original complaints. Writing for the majority, Justice Sandra Day O'Connor noted that teachers and coaches "are often in the best position to vindicate the rights of their students because they are better able to identify discrimination and bring it to the attention of administrators." *Id.* at 1508.

As a result of the Court's decision in *Jackson*, public schools, colleges and universities that receive federal funding should train their administrators to respond to complaints of Title IX violations and educate them on the prohibition on retaliation. These institutions should also review their complaint procedures to ensure that students and employees are allowed to complain about perceived sex discrimination whether or not they are subjected to the purported discriminatory practice or conduct. As with other complaints of discrimination, administrators should respond promptly to investigate any claims that the institution is violating Title IX. In addition, education employers and public schools should review their financial support to athletic teams as well as the scheduling of practices and games to rectify any inequities.

Are Attorneys Fees for Successful Employment Discrimination Claimants Taxable Income?

Commissioner v. Banks, 125 S.Ct. 826 (decided January 24, 2005)

In *Commissioner v. Banks*, 125 S.Ct. 826 (2005), the Supreme Court addressed the question of whether the portion of a money judgment or settlement paid to an attorney under a contingent-fee agreement is income under the Internal Revenue Code, 26 U.S.C. §§ 1, *et seq.*

The ruling concerned two consolidated cases: taxpayer Banks settled his federal employment discrimination suit against a California state agency and taxpayer Banaitis settled his Oregon state case against his former employer. Neither taxpayer included fees paid to attorneys under contingent-fee agreements as gross income on their federal income tax returns. The Commissioner of the Internal Revenue issued a notice of deficiency, which the Tax Court upheld. In Banks' case, the Sixth Circuit reversed in part, finding that the amount Banks paid to his attorney was not includable as gross income. In Banaitis' case, the Ninth Circuit held that because Oregon law grants attorneys a superior lien in the contingent-fee portion of any recovery, that part of his settlement was not includable as gross income.

The Supreme Court held that when a litigant's recovery constitutes taxable income, such income includes the portion of recovery paid to the litigant's attorney as a contingent fee. *Id.* at 829. The Court applied what is known as the "anticipatory assignment of income" doctrine, which provides that one who earns or has control of income cannot escape being taxed on that income even if he or she assigns it to someone else.

The Supreme Court's decision in *Banks* might have made settling cases significantly more expensive for employers were it not for the American Jobs Creation Act of 2004, 118 Stat. 1418 ("AJCA"). The AJCA alleviated the effect of *Banks* by amending the tax code to allow a tax payer, in computing adjusted gross income, to deduct "attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with any action involving a claim of unlawful discrimination." 26 U.S.C. § 62(a)(19).[2] The AJCA defines "unlawful discrimination" to include a number of specific federal anti-discrimination statutes, any federal whistle-blower statute, and any federal, state, or local law "providing for the enforcement of civil rights" or "regulating any aspect of the employment relationship … or prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted by law." *Id.* §§ 62(e)(1) to (18).

As a result of the AJCA, a victorious plaintiff must still report the entire settlement or judgment as taxable income, but he or she is required to pay tax only on the amount actually received and may deduct the attorneys fees incurred in prosecuting his or her employment discrimination suit. Because the AJCA allows an above-the-line deduction as opposed to an itemized deduction, the deduction is also allowed in computing the plaintiff's alternative minimum tax liability. The AJCA is effective for costs and fees paid after October 22, 2004 for any judgment or settlement occurring after that date.

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[2] The two cases in *Banks* arose before Congress enacted the American Jobs Creation Act, which is not retroactive. As the Court noted, these cases would not have arisen had the Act been in force for the transactions at issue. *Banks*, 125 S.Ct. at 830.

In light of the AJCA, the Supreme Court's decision in *Banks* applies only to cases involving allegations of employment discrimination that were settled or received a judgment prior to October 22, 2004. With respect to pre-AJCA settlements or judgments, successful employment discrimination plaintiffs are not precluded from arguing that fee shifting is appropriate and the court should thus require the employer to pay the plaintiff's attorneys fees if the plaintiff wins thereby excluding this portion of the award from plaintiff's taxable income. The Court in *Banks* did not consider the fee-shifting provision of antidiscrimination laws because the *Banks* fees were paid to the attorney under a contingent fee agreement and were not awarded by the court.

The overall impact of the AJCA benefits both employees and employers. While employees will be able to shelter a potentially large portion of a settlement or award from taxable income, employers will benefit because the cost of settling employment discrimination claims should be reduced due to the fact that plaintiffs cannot bargain for a higher settlement under the rationale that they must offset an obligation to pay taxes on their attorney's fees portion of the settlement.

Issues to Watch: The Supreme Court's 2005-06 Docket

The Supreme Court's 2005-06 term officially began on Monday, October 3, 2005. In the first oral argument of the new term, the Court heard two consolidated cases questioning whether the Fair Labor Standards Act of 1938, 29 U.S.C. §§ 201, *et. seq.* ("FLSA"), requires that workers be paid for the time spent between two principal activities. In addition, the Court has agreed to hear another employment case involving the statutory minimum employee threshold under Title VII as it relates to the subject matter jurisdiction of federal courts.

Compensable Time under the FLSA

Alvarez v. IBP, Inc., 339 F.3d 894 (9th Cir. 2003), *cert. granted*, February 22, 2005, 125 S.Ct. 1292 (Nos. 02-35042; 02-35110) and *Tum v. Barber Foods, Inc.*, 360 F.3d 274 (1st Cir. 2004), *cert. granted* February 22, 2005, 125 S.Ct. 1295, 2005 (Nos. 02-1679; 02-1739) .

In the first argument of the new term, the Supreme Court heard two consolidated cases addressing whether the Fair Labor Standards Act of 1938, 29 U.S.C. §§ 201, *et. seq.* ("FLSA"), as amended by the Portal-to-Portal Act, 29 U.S.C. § 254 ("Portal Act"), requires that workers be compensated for the time spent between two principal activities: donning or doffing required safety equipment and beginning or ending actual work inside meatpacking and chicken processing plants.

In *Alvarez v. IBP, Inc.*, 815 meatpacking employees sued their employer under the FLSA alleging that the employer was required to pay them for the time it took to change into required specialized protective clothing and safety gear as well as the time spent walking to and from plant stations after donning or doffing personal protective equipment. After a bench trial, the United States District Court for the Eastern District of Washington granted judgment in favor of the employees, and the Court of Appeals for the Ninth Circuit agreed in part but failed to uphold the entire damage award. It found that the employees' actions of donning, doffing, and retrieving job-related protective gear before and after working on production lines were "integral and indispensable" activities "necessary to the principal work performed and done for the benefit of the employer." *Id.* at 902-03. Thus, these activities were compensable under the FLSA. The Ninth Circuit also found that the time the employees spent walking to and from plant stations where mandatory protective equipment is distributed was compensable. Both the

district court and the Ninth Circuit agreed that, although the time spent waiting at and walking to these stations might be considered "preliminary and postliminary," such activities are still compensable because they are "integral and indispensable" to the employees' jobs. *See Alvarez v. IBP, Inc.*, 339 F.3d 894 (9th Cir. 2003).

The Court of Appeals for the First Circuit came to a different conclusion when presented with similar facts in *Tum v. Barber Foods, Inc.*, 360 F. 3d 274 (1st Cir. 2004). In *Tum*, poultry plant workers sued their employer under the FLSA seeking compensation for time spent waiting in line for required clothing and safety equipment and time spent walking from the area where they obtained required clothing to the area where they obtained additional items. Following a jury trial, the United States District Court for the District of Maine found that the employer was not required to compensate the 300 employees at its poultry processing plant for the time spent waiting and walking to stations where required health and safety gear is distributed. The First Circuit affirmed, concluding that these tasks were "preliminary and postliminary" activities exempted from compensation. 360 F.3d 274 (1st Cir. 2004).

The Supreme Court granted certiorari on the issue of whether an employee is entitled to compensation for time spent waiting at stations where required safety and health equipment is distributed, donned, and doffed, and traveling to and from these stations to work sites at the beginning and end of each workday. It did not consider whether time spent actually putting on or taking off the safety gear was compensable. Under the FLSA, employers must compensate employees for all of the time which the employer requires or permits employees to work. However, the Portal Act removed employers' obligation to compensate employees for activities which are "preliminary or postliminary" to an employee's principal activities unless they are an "integral and indispensable part of the principal activities for which covered work[ers] are employed." 29 U.S.C. § 254(a)(2). In addition, the Portal Act exempts from compensation "walking, riding, or traveling to and from the actual place of performance of the principal activity or activities which such employee is employed to perform." *Id.* § 254(a)(1). The employees in both *Tum* and *Alvarez* argue that waiting at the safety stations and walking to and from these stations are inextricably linked to the donning and doffing process, and are thus "principal activities" for which they must be compensated. They also contend that because these activities occur within the workday, the Portal Act exceptions do not apply.

At oral argument on October 3, 2005, the companies argued that the Portal Act was intended to exempt the walking and waiting at issue in these cases. While the companies conceded that the time the workers spend donning and doffing required safety equipment is "integral and indispensable" and thus compensable, they maintained that the employees' principal activity is meat processing and not donning safety gear. According to the companies, donning safety equipment does not trigger the start of the workday and necessitate compensation for walking or waiting that follows. A majority of the justices appeared unwilling to deviate from precedent on this issue established in *Steiner v. Mitchell*, 350 U.S. 247 (1956), in which the Court found that "activities performed either before or after the regular work shift" are compensable "if those activities are an integral and indispensable part of the principal activities." *Id.* at 256. Justice Roberts suggested that the companies' analysis of *Steiner* would create a third category of activity: that which is "integral and indispensable" and thus compensable but not principal and does not trigger the start of the workday. The Supreme Court seemed unwilling to form this third category.
The Supreme Court's ruling on these conflicting decisions will involve important public policy matters, such as employee safety. The Court's decision could also dramatically affect workers' salaries and manufacturing costs.

If the Court sides with the employees and expands the definition of "principal activity" to include waiting and walking, such a ruling could also entitle employees to compensation for time spent retrieving required uniforms and equipment in other occupations where employees are required to wear specific uniforms and equipment, such as police officers, nurses, and construction workers.

Can Title VII's 15-Employee Requirement Keep You Out of Federal Court?

Arbaugh v. Y&H Corp., 380 F.3d 219 (5th Cir. 2004), *cert. granted* May 16, 2005 (No. 03-30365).

The Supreme Court is scheduled to hear argument in 2006 on an appeal from the Fifth Circuit on the question of whether a Title VII's plaintiff's failure to qualify a defendant as an "employer" under Title VII deprives a federal district court of subject matter jurisdiction.

In *Arbaugh v. Y&H Corp.*, 380 F.3d 219 (5th Cir. 2004), a former waitress/bartender brought an action against the restaurant where she worked and one of the restaurant owners alleging sexual harassment under Title VII. Defendants moved to dismiss on the ground that the restaurant did not qualify as an "employer" under Title VII, because it did not employ fifteen or more employees for twenty or more calendar weeks during the relevant time period. *See* 42 U.S.C. § 2000e(b). The district court agreed that it did not have subject matter jurisdiction and dismissed the plaintiff's case.

On appeal, Arbaugh argued that the issue of the number of employees Y&H employed during the relevant time period goes to the merits of an employment discrimination case and is not a jurisdictional issue. She relied on precedent from the Second, Seventh, and Federal Circuits, which have all found that the number of employees employed by a defendant is not a jurisdictional question but goes to the merits of the case. However, the Fifth Circuit, along with the Fourth, Sixth, Ninth, Tenth, and Eleventh Circuits have all concluded that the "employer" definition creates a jurisdictional requirement. The Fifth Circuit rejected Arbaugh's argument that the census issue is not jurisdictional and upheld its prior precedent in concluding that the number of employees determines a court's subject matter jurisdiction in a suit filed pursuant to Title VII.

The Supreme Court's decision in *Arbaugh* will affect a wide range of small business employers. Its ruling will impact not only Title VII cases, but will also implicate other anti-discrimination statutes with numbers requirements such as the Americans with Disabilities Act, the Age Discrimination in Employment Act and the Family Medical Leave Act. If the Supreme Court upholds the Fifth Circuit's decision and finds that federal courts lack subject matter jurisdiction to hear Title VII claims where the defendant employs less than fifteen employees, plaintiffs will be required to bring discrimination claims against these employers under state law in a state forum. In addition, businesses with less than fifteen employees will not be able to remove such claims to federal court unless there is another ground for federal jurisdiction such as diversity of citizenship or another federal law at issue.