NYSBA
WINTER 2010 | Vol. 28 | No. 3

Inside

A publication of the Corporate Counsel Section
of the New York State Bar Association

Message from the Chair

On behalf of the Executive Committee, I am so happy to share with you some of the recent activities that the Section has been working on and ways in which you can get involved.

Since our last edition of *Inside*, the Kenneth G. Standard Diversity Internship Program has been completed for the summer 2010 session, and was a great success. We've included a photo of the reception. A special thank you to Executive Committee Member Anne Atkinson, and her firm, Pryor Cashman LLP, for her time and donating a beautiful space for the event. And again, I would also like to thank the Internship Committee for all of their hard work.

In September, we held our first Member Appreciation Reception, which had a terrific turnout. Thank you to Tom Reed and the Membership Committee for their work on the event, and to Gensler for donating the space. Please be on the lookout for our End of the Year Reception, which will be held on December 8th at Executive Committee Member Gary Roth's firm, Broadcast Music Inc. (BMI). Space will be limited and admission is complimentary.

On October 19th, we partnered with the International Section's Corporate Counsel and Compliance Committees to hold a CLE on new developments in the Foreign Corrupt Practices Act, which was geared towards Corporate Counsel. Special thanks to Duane Morris for donating space for the event, and to the team who organized the event and presented the materials. We had a great response to the event and have heard wonderful feedback from the attendees. If you would

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Editors: Janice Handler and Allison B. Tomlinson

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like a copy of the materials from this event, please feel free to contact us.

We also recently held our signature Ethics for Corporate Counsel Program on November 12th. It was a great success and extremely well received.

Last, we have been working closely with Lexology to bring our members a service that will email you case summaries and up-to-date information on various areas of the law. You will be able to tailor this e-blast to suit your individual needs, including setting the topics, frequency, etc. We will send you more information shortly.

Thank you for your interest in the Section. We are here for you, so please feel free to call or email us at the contact information listed on the last page of *Inside* with your ideas and thoughts.

All the best,
Allison B. Tomlinson

A Dozen Important Employment Law Considerations for In-House Counsel

By Joel J. Greenwald

In my practice—advising and representing management in labor and employment law matters—I've seen a lot of "unnecessary" litigation. It's unnecessary because it could have been avoided—or at least mitigated—had the company made fairly simple changes to its employment practices and agreements. As in-house counsel you have a multitude of issues on your plate already. Corporate transactions are under closer scrutiny than ever. But it makes sense to add employment practices to your list of areas to monitor and review because this is one where lawsuits can potentially be avoided. The ROI for your time spent in heading off claims and lawsuits before they arise, or in setting the stage for defenses against lawsuits that do occur, is enormous.

Here are a dozen important employment law considerations for in-house counsel.

Exercise Caution When FMLA Leave Is Over, and the Employee Still Needs Medical Leave

Under the Family and Medical Leave Act ("FMLA"), covered employers must provide up to twelve weeks of unpaid leave to qualifying employees due to their own serious medical issues. Life, however, is rarely "neat"—there is a good chance that an employee may need further leave after he or she uses up the requisite twelve weeks.

Don't rush to terminate the employee just because he or she can't yet return to work, or because the employee can return part-time, or needs intermittent time off for continuing medical treatment. If the employee's condition would constitute a disability under applicable law, the employer may need to provide further leave as a reasonable accommodation. If you don't provide the reasonable accommodation, or if you terminate employment or take other adverse employment action because of the employee's need for leave, you may be violating anti-discrimination laws.

It's also vital to look to state disability law as well as federal. States promulgate their own laws regarding disabled employees and leave, which could provide more generous leave or be more protective of the employee than federal law. In fact, as a general matter—*always* look at state (and sometimes city) law as well as federal regarding *any* employment or labor law issue.

Store Signed Employment Agreements in a Multitude of Places

Written employment agreements, such as non-competition or confidentiality agreements, are vital. In the event of a dispute with a current or former employee, the agreement can often be the difference between prevailing or not.

Of course, it doesn't matter *what* an agreement's terms are if you can't locate the signed agreement when needed. Not only does critical paperwork seem to have a proclivity to get lost at the least opportune moments, but employment agreements may be targeted by unscrupulous employees for theft or modification.

Just as you back up critical computer data or files, you need to "back up" employment agreements. In addition to scanning the signed agreements onto the company's computer system, multiple copies should be kept in secure locations, such as in counsel's office as well as in the HR department and also in the office of a manager with a legitimate need for the contract. By avoiding the possibility of the "loss"—whether accidental or not—at a critical time, you make sure that your company can take advantage of the contract's bargained-for terms.

Watch Your Subcontractor's Labor Practices… Because You May Incur Joint Employer Liability for Their Wage and Hour Failures

Even experienced counsel may believe that a contractor relationship insulates their company from liability arising from their subcontractors' employment practices. However, it's not nearly that cut-and-dried. In employment law, agencies and courts look past the relationship's formal structure to how it actually played out in the real world, to determine which companies may be an individual's employer and thus responsible for his or her compensation.

For example, the Second Circuit, in *Zheng v. Liberty Apparel Company, Inc.*[1] concluded that it was possible for a garment manufacturer which subcontracted out part of the manufacturing process to be a "joint employer" of its subcontractors' employees. There, the subcontractors were separate legal entities, with separate ownership, and had executed contractor agreements with the manufacturer. However, the manufacturer exercised control over the subcontractors' workers by sending its own staff to inspect and supervise the manufacturing process. Thus, the manufacturer was found to be a joint employer of the subcontractors' employees and thus liable for any labor law violations committed by its subcontractors—such as a failure to pay overtime wages.

In this arena, contracts and agreements are probative but not dispositive. It's vital to both make sure that any contractor-subcontractor relationship is sufficiently arm's length to support the subcontractor characterization. However, it's impossible to rule out 100% that you might be found to have a joint-employer relationship in the event of an employee lawsuit. Therefore, it is a good practice to ensure that your subcontractors obey the law and employ appropriate labor practices.

Preserve Computer Hard Drives Whenever a Problem Employee Leaves

Employees' computers are often the best source of evidence for what they have been doing when they were supposed to be working. The hard drive contains not only all the files, both personal and professional, that an employee saved, but also "temporary" Internet files that can evidence browsing behavior. Back-up copies of emails and other electronic communications, even files that the employee thought had been deleted, can also be restored.

"Deleting" files does not actually "delete" them—it just removes the file's address so it can't be readily found. It's analogous to removing the file tab, with the folder name on it, from a hanging folder and dropping the folder into some non-obvious location in your office. That makes it difficult to find, but not impossible. Just as a dedicated search could turn up that folder, so can "deleted" files be retrieved from a computer unless the hard drive was overwritten to military erasure standards.

If an employee was a problem, you may need evidence for litigation later—either (a) for defensive litigation, if sued by the employee or by someone the employee injured, or (b) in the event you elect to sue the employee, such as for misappropriation of confidential information. Preserving the hard drive upon an employee's termination affords the opportunity to see if the employee had work files he or she should not have had, had inappropriate images or other content on the company's computer, or sent inappropriate messages or data to competitors.

Know How and When to Use the Police with Regard to Employee Theft Issues

Theft—including theft of intellectual property—is of course a crime as well as a civil tort. However, while it might seem straightforward to involve the police when a criminal act has been committed, there are two important considerations to bear in mind.

First, if you're going to report the employee to the police, then do so. Under no circumstances, however, should you threaten an employee with filing criminal charges "unless" he or she takes some action such as return the stolen item(s), identify coconspirators, etc. If you do this, you may be committing extortion or blackmail and incurring your own criminal liability. It also may be against the law to use the threat of criminal charges in these circumstances.

Second, under your business's insurance policy, you may be required to report theft to the police if you're going to make an insurance claim. If you fail to do so, the insurance may not cover. As soon as you suspect a crime, you should review your policies to see whether you are covered for this act, to what extent, and what actions you need to take to preserve your coverage.

Make Sure New Employees Verify That They Are Not Bringing Any Trade Secrets with Them, and Also Verify Whether They Have Non-Competition (or Non-Solicitation) Agreements in Force

Many employees are hired from the competition, either deliberately—to weaken the competition and take advantage of their talent—or simply because that's where you find experienced personnel. This, though, creates two risks:

- *Has the employee brought any trade secrets or other confidential information?* If so, and if it's used on behalf of your company, you could find yourself complicit in theft of trade secrets and subject to lawsuits for monetary damages and/or injunctive relief.
- *Is the employee subject to a non-competition or non-solicitation agreement?* If so, your company could be subject to monetary damages for the employee's breach of agreement, and the former employer could sue to enforce the agreement and obtain an injunction requiring you to fire the new hire, depriving you of that employee's services, indirectly costing you money (*e.g.,* time and money spent on recruitment and training), and also disrupting your projects or operations.

Before new hires start, have them execute an agreement stating that they will not use any trade secrets, know-how, or confidential information from prior employers and also that they are not subject to any non-competition or non-solicitation agreements. This will do several things:

1. Put the employee on notice to not use any former employers' trade secrets;
2. Get you the information you need to make an informed decision as to whether to hire the applicant (*e.g.,* if you find out there is a non-competition agreement, you can review it and decide whether to go ahead with the hiring);
3. Help insulate you from liability, by showing that you took reasonable precautions and neither intentionally nor even negligently trespassed on another's trade secrets; and

4. Give you grounds to sue the employee, if he or she causes you monetary losses in this fashion.

Don't Punish People by Taking Away Wages Owed

Employees work for pay. It's tempting to punish them for poor performance or for actions which cost the company money by taking away their wages.

However, doing so is a violation of labor law. While there are many things that an employer can do to punish an employee for work-related issues—*e.g.*, termination, suspension, demotion, or a forward-looking reduction in pay—employees must be paid for all work actually performed to date. Failure to do so may violate various statutes, such as, for example, § 193 of New York State's Labor Law, which only allows paycheck deductions for certain specifically defined reasons, other than taxes, (such as for health insurance premiums), when authorized in advance in writing.

Many employers make the wrong choice and withhold a final paycheck—or set the amount off against the value of property that has not yet been returned. Paychecks must be paid on a regular basis. Failure to do so opens you up to legal action.

You can never legally punish an employee by taking away wages already earned. Nor can wages be deducted in New York for damaged goods or company property that is not returned.

Make Sure You Have Written Commission Agreements with Your Salespeople

As any experienced attorney knows, many contractual disputes arise out of nothing more than differing recollections of the terms of an oral or not-well-documented agreement. Setting forth all terms with specificity, in writing, in advance, is arguably the simplest and yet most powerful action most counsel can take to avoid later litigation.

This is doubly true for commission agreements. In many states—New York being one—in the event of a commission dispute, the courts will defer to the employee's position or recollection of the terms if there is no written agreement or an ambiguous one. Given this presumption, it's imperative for employers to protect themselves against later disputes by setting down all the terms of the agreement in writing, as precisely as possible.

This includes the situation of giving salespersons some additional "kicker" or incentive. It's fine to encourage a salesperson to sell harder by offering something extra—but make sure that the specifics of what has to be done to earn it is spelled out. Address how commissions are paid when employment is terminated.

Do not assume any term is obvious or can go unsaid. For example, it may be common practice to debit commissions for returns and bad debts—but "common practice" may not be enough to rely on, if the salesperson disputes a deduction. If the agreement specifies that there will be charge backs in the event of unconsummated or uncollected sales, the salesperson will be hard-pressed to dispute the deduction later.

Managers Have to Be Trained How to Handle Internal Complaints

Your company's managers are your first line of defense when it comes to employee complaints, including discrimination and harassment complaints. If they are not trained in how to respond to these complaints, then there is every chance that they will make the situation worse, either by not responding or by responding inappropriately.

There's no way to eliminate your company's managers from the complaint process. First, as a practical matter, they are often the ones that employees turn to when there is a problem or issue. An employee is more likely to go to his or her supervisor (assuming the supervisor is not the problem) than to in-house counsel or a designated senior executive.

Second, a well-designed discrimination or harassment policy *must* have multiple avenues of complaint. One of those avenues should be your company's managers.

For that reason, no matter how well *you* and your staff (or HR) know how to deal with internal complaints, if your managers don't understand what to do and say, or don't even recognize that the complaint can have a legal effect on the company, your company's policy and response will be *de facto* inadequate. It is incumbent on you to make sure that managers know how to handle these situations—especially since these complaints often come up in the *worst* context for good extemporaneous decision making. Making sure that managers are thoroughly prepared will help ensure the complaints are handled in a prudent, appropriate way to legally protect the company.

Make Sure Your Severance Agreements Are Valid

While employers and employees can bargain for almost anything as part of severance agreements—the amount of severance (if any), continuation of benefits, etc. (presuming no policy governs the benefits)—there are some statutory limitations on these agreements.

First, ensure that the terms of the Older Workers Benefits Protection Act are complied with. This means, for example, providing an "older" worker—*i.e.*, one who's over 40 years old, though 40 hardly seems "old" anymore!—at least 21 days to consider or review the agreement and 7 days post-signing to revoke it. If the separation is part of a reduction in force, the "older" employee must be given at least *45 days* to consider the agreement before signing it. In addition, there are various other drafting and notification requirements, such as drafting the agreement in "plain English," advising the employee that he or she can have counsel review the agreement, and making sure the employee understands that by signing, potential claims under the ADEA (Age Discrimination in Employment Act) are being waived.

Second, remember that employees may *not* waive potential claims under the Fair Labor Standards Act (FLSA). It doesn't matter what consideration you offer or how voluntary and informed such waiver is—the law does not allow people to contract away their rights to make claims for unpaid wages or overtime.

Don't Access Your Employees' Personal Email or Social Media Accounts; Any Monitoring Should Be Pursuant to a Consent Policy

Companies have considerable latitude to monitor their employees' electronic communications or company equipment. However, "considerable latitude" is not "unbridled discretion"—there are still limits companies must respect.

- *Do not access personal email or social media accounts.* It's important to not confuse work or business email (*i.e.*, email accounts which the company has provided for its staff—which a business *may* access), and personal email accounts or social media (*e.g.*, FaceBook, MySpace) which belong to an employee. The right to access and monitor communications made through employer-provided email or other platforms does not necessarily translate to a right to access the employee's personal accounts and email—even if the employee accessed those sites on company equipment. Doing this could lead to liability for violation of privacy.
- *All monitoring must be pursuant to a consent policy*. To defeat any expectation employees may have regarding their use of company computers, companies should promulgate a computer and monitoring policy (*e.g.*, stating that the company can monitor all email or web-browsing on company systems). This policy should be both explicitly agreed to, in writing by staff, and made a term or condition of employment, so that, by working there, the employee is deemed to have given consent to monitor and acknowledges he or she can't have an expectation of privacy. By having a strong consent policy and obtaining proof that employees saw and agreed to the policy, you can avoid challenges over company monitoring its computer systems.

When Conducting Video Surveillance, Don't Record Any Audio

Workplace video surveillance, with proper notice and of permissible locations, is allowed. However, recording audio in the workplace is *not*. If you make audio recordings, you can run afoul of various laws, including wiretapping statutes.

While workplace video surveillance is permissible, it's important to do it properly. It is also optimal to provide no surveillance in private areas—locker rooms, etc.

The Importance of Active Counsel

There are areas of law in which it's impossible to eliminate liability. In employment law, however, it is possible to eliminate many, if not most, sources of concern. Employer liability typically arises from violations of employment laws or improper practices, often by managers not trained to operate otherwise. They violate employee privacy, fail to provide reasonable accommodations, or don't report a harassment complaint. By paying attention to the potential pitfalls in advance, the prudent general counsel keeps the employer from being unprepared should a lawsuit, theft or other unforeseen event occur.

DISCLAIMER: The foregoing is a summary of the laws discussed above for the purpose of providing a general overview of these laws. These materials are not meant, nor should they be construed, to provide information that is specific to any law(s). The above is not legal advice and you should consult with counsel concerning the applicability of any law to your particular situation.

Endnote

1. __F.3d__, No. 09-4890- CV, 2010 WL 3119915, (2d Cir. Aug. 10, 2010).

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Worker Misclassification: A Trap for the Unwary

By Richard A. Levin

Particularly in recent difficult economic times, companies have increasingly turned to "independent contractors" to serve as a supplemental workforce. One study estimated that as many as 30% of the workers classified as independent contractors were actually employees, and that figure may even be higher now. Use of independent contractors saves taxes and employee benefit payments, and makes for easier workforce adjustments as needs change. Such a course is, however, fraught with danger.

Enhanced Risks in Use of Independent Contractors

Recently, numerous government agencies have made it clear that they are giving independent contractor arrangements enhanced scrutiny. For example, the Internal Revenue Service reportedly plans to hire as many as 6,000 new agents to audit companies in search of misclassification of employees as independent contractors. The U.S. Department of Labor also has requested significantly greater budget allotments to permit it to seek out cases of worker misclassification. In New York, the state Department of Labor has, for several years, been focused on remedying the misclassification of employees as independent contractors, and has created a multi-departmental task force to address such misclassification.

Moreover, legislative initiatives are ongoing at various levels to address the issue of worker misclassification. On the federal level, the proposed Employee Misclassification Prevention Act (EMPA, H.R. 107, S. 3254) would greatly increase the record-keeping burden on companies. Employers would be required to specifically notify workers of their status as employees or as non-employee contractors. EMPA also would call for greater coordination between IRS and the Department of Labor, with targeted audits, especially in industries with high concentrations of misclassification, and the penalties for misclassification would include a payment of $5,000 per offense in the case of willful violations, in addition to the current requirement that the misclassifying employer pay 3% of the salary of the misclassified worker as income tax withholding, plus pay the employer and the employee share of FICA. The proposed Taxpayer Responsibility, Accountability and Consistency Act (TRAC, H.R. 3408, S. 2882) would increase the penalties for companies that file tax returns with inaccurate classification information, and would also eliminate the "safe harbor" present in IRC § 530, which currently allows employers to avoid penalties for good faith misclassification of certain workers as independent contractors. TRAC would also allow individuals to petition the Secretary of Treasury for a determination of their status as independent contractors rather than employees.

At the state level, New York enacted the Construction Industry Fair Play Act, which adds a new article (Art. 25-B) to the state Labor Law, creating a rebuttable presumption that all construction workers are employees. (Labor Law §861-c.) The act also mandates notice posting, and subjects violators to civil penalties and potential criminal liability. This new law took effect October 26, 2010.

From a governmental standpoint, this enhanced scrutiny makes sense. Misclassification deprives governments of an important source of revenue from employment taxes, FICA, unemployment insurance contributions and workers' compensation premiums. From an employer standpoint, however, the stepped-up enforcement initiatives and new legislation create a potential nightmare.

Any company found to have misclassified employees as independent contractors faces a plethora of liabilities. To begin with, such a company could be subjected to federal and/or state wage and hour penalties. Under the federal Fair Labor Standards Act, if a worker is found to be an employee, and has worked more than 40 hours in a week, the worker is entitled to time-and-one-half overtime pay for all of the time worked in excess of 40 hours in a week. The FLSA permits recovery going back two years (three years in the case of a willful violation), and provides for additional liquidated damages equal to 100% of the unpaid wages. New York state's Labor Law also requires overtime premium pay for employees who work more than 40 hours in a week, and permits recovery going back six years, with a 25% penalty. Attorneys' fees are also recoverable. This wage and hour exposure may result in massive liability for even a relatively small employer.

Additionally, there are federal employment tax implications that stem from misclassification. If an employer fails to properly withhold federal, state or local income taxes from the wages of a worker who is held to have been misclassified as an independent contractor, that employer can be found liable for unpaid income taxes, plus interest and penalties. The employer would also be liable for the employer and employee portions of FICA and FUTA. Similarly, the state is likely to seek to collect unpaid unemployment insurance and workers' compensation premiums, plus potential interest and penalties based on employer's failure to pay those premiums in a timely manner.

Misclassification of employees may also create an immigration issue. Employers are required to maintain

I-9 forms for all employees. Assuming that the employer does not have an I-9 form for a worker misclassified as an independent contractor, penalties and fines are likely to be imposed.

Often, the most significant impact of misclassification arises with regard to employee benefit plans. Take, for instance, the case of *Vizcaino v. Microsoft Corp.*,[1] a case that generated a great deal of publicity in the legal and popular press. The court found that a large number of independent contractors at Microsoft were, in fact, employees, and, therefore, were entitled to coverage under Microsoft's pension plan, just as employees were covered. The resultant cost to Microsoft's pension plan was enormous. Failure to cover a substantial number of misclassified workers under a pension plan may also expose the plan to loss of its tax-qualified status.

Independent Contractor vs. Employee

The potential for monumental damages and penalties makes it essential that any enterprise takes all reasonable steps to make certain that it has correctly classified its workers, and that whatever governmental entities may be involved will agree that those workers classified as independent contractors are, in fact, contractors and not employees. There are certain steps that a company may take when entering into an independent contractor arrangement that should increase the likelihood that that arrangement will pass muster.

It is helpful to enter into a written agreement with the independent contractor. Such agreement should:

- Specify the discrete tasks for which you are contracting, not a time period or amount of work;
- Base compensation on completion of the tasks contracted for, not on the amount of work performed;
- Limit the engagement to a specific, closed-ended term or project;
- Specify milestones toward the completion of the project, but avoid daily or weekly reports or any reference to work hours or work schedules;
- Allow the contractor to determine when and how the work is to be performed;
- Specifically allow the contractor to perform similar work for other companies, even while the engagement is in effect;[2]
- Explicitly state that the contractor is not covered by the company's liability or workers' compensation insurance or other employee benefits; and
- Include a provision that the contractor will indemnify the company for taxes, benefits or other liability if the contractor is determined to be an employee.

Having such a written contract is a useful step in establishing an independent contractor relationship, but the contract, alone, will not satisfy a government auditor or a court. Rather, the classification of the individual as a contractor or an employee will depend primarily on how the relationship actually functions. No single factor is determinative, but the overwhelmingly most important factor is ***control***—to what extent does the company control the work of the contractor?

Certainly, a company can, and should, set quality standards for its contractors. But a company that dictates how the contractor performs the tasks, where the tasks are performed, and the time in which they are performed, is more likely than not going to find itself with an employee rather than a contractor.

Factors that are likely to be considered in determining classification include:

- Whose tools or equipment are being used? A contractor who uses his or her own tools and equipment is more likely to be accepted as a contractor than one who uses the company's equipment.
- Where is the work performed? A contractor who sits in the office next to regular employees is more likely to be deemed an employee than one who works away from the company's workplace, reporting to the company only occasionally as needed by the nature of the project.
- Does the contractor have a significant investment in the contracting business, and does he or she stand to make a profit from the operation of the business?
- Are contractors clearly distinguished from employees? Including contractors in company telephone directories; providing them with business cards with the company's name on them; or giving them company e-mail accounts will all increase the likelihood that the contractor will be deemed to be an employee. If ID cards are required, try to make the ID cards for contractors readily distinguishable from those of employees.
- Who supervisors the contractors? A contractor who is subjected to time and attendance recording or discipline by the company's supervisors in a manner similar to that applicable to regular employees is more likely to be deemed an employee than one who is generally free to come and go at will, and who is responsible only to finishing the task for which he or she was contracted. Similarly, performance reviews of the contractor should be avoided (although periodic reviews to determine whether the contractor is meeting the benchmarks for completion of the project are appropriate).
- Does the contractor need training? Presumably, the company is contracting with the contractor because

of the contractor's expertise and ability. The contractor should not require extensive training from the company, beyond that orientation necessary to mesh the contractor's knowledge and skills to the particular needs of the company.

- How long will the contractual relationship continue? To the extent that the contractual relationship becomes protracted, that relationship tends to take on more of the characteristics of employment than of a contract. In no event should the contractual relationship extend beyond the completion of the project for which the contractor was retained. Contractors who are retained for sequential projects extending over the course of many years are likely to be deemed to be employees.

In this regard, it is helpful to contract with people who are in the business of providing the service for which you are contracting, and who have established businesses providing such services, rather than "freelancers." In many cases, one of the first things that an auditor does when looking at worker classification is to try to determine whether the contractor holds himself or herself out as being in business—is the contractor incorporated?; does it have an ad in the yellow pages or other business directories?; does it have a company name and letterhead and business cards in that company name?; does it have an employer tax identification number for its business?; does it submit invoices for payment?; are there other indicia that the contractor functions as a separate business?

Sometimes a company will continue using the services of a retired former employee as a contractor. Such an arrangement is often useful to the company, because it permits the company to continue to have access to specialized knowledge and experience, and it is useful to the former employee, because it eases the former employee's transition from work to retirement. However, such arrangements may pose problems of misclassification. It is often difficult to explain to the satisfaction of a government auditor how an individual who is performing virtually the same functions as he or she had been performing as an employee, is now performing those functions as an independent contractor. Where such an arrangement with a former employee is necessary, great care should be taken to assure that the arrangement is carefully delineated for a limited duration. It may be advisable to have the former employee come back not to perform the work—but rather as an instructor, to teach his or her replacement how to do the work.

In some cases, risk of misclassification may be mitigated by contracting with an agency to provide the needed service, rather than contracting with an individual worker or sole proprietor of a business. Use of an agency to provide the worker adds an element of separation between the contracting company and the worker, particularly if that worker is treated as an employee of the agency. However, even in those situations where an agency serves as an intermediary, excessive control by the company contracting for the services may convert that company into a joint employer of the worker.

Conclusion

The distinction between an independent contractor and an employee is a highly factual one. Misclassifications are common, and enforcement by governmental entities at all levels is surging. It behooves any employer to use extreme care in structuring any arrangement with a contractor to increase the likelihood that the desired classification will withstand challenge.

Endnotes

1. 120 F.3d 106 (9th Cir. 1997).
2. If there is a concern about trade secrets, the company may wish to include a confidentiality or non-disclosure provision, but caution should be exercised, because in some cases such provisions have been considered an indicator of employee status.

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Violence Lurks Where You Work

By James R. Redeker

According to the Bureau of Labor Statistics, between 1997 and 2009, there were 8,127 homicides in American workplaces. Of this number, 6,169 were by robbers and other strangers, 1,377 were by other employees or customers, 581 were by family members or other personal acquaintances. Each of the categories of perpetrators of workplace homicides presents different considerations for employers:

- Strangers rarely engage in indiscriminate killings. Rather, they usually are intruders with a purpose other than committing a homicide (e.g., robbery, rape).
- Employees, former employees or customers usually seek retribution or revenge for perceived wrongs. They may or may not have a specific target in mind, such as the manager responsible for a termination of employment decision. Even if they have a target, other employees in the area are at risk of injury or death.
- Family or personal acquaintances may enter the workplace to continue or end a domestic dispute or some other problem unrelated to the workplace.

Regardless of the category of perpetrator, survivors of those who are murdered or injured may seek to have the employer held liable and, at some point on the responsibility continuum, they will succeed if the employer's conduct falls below what society would expect from a reasonable person. If an employer, in light of the nature of the work an employee would do, hired an applicant that a background check would have suggested would be an unacceptable risk to other employees or customers, the employer may be liable for the effects of the employee's violent acts under a theory of negligent hire. Similarly, an employer may be liable for the violent acts of an employee who, by conduct in the workplace, gave notice to the employer that she was a threat to other employees. Finally, employers may be liable for the death or injury of an employee where the danger could be foreseen because of where the employee is required to be while performing his job.

Even where an employer escapes legal liability, profound remorse, questioning and guilt weigh heavily on any employer when its workplace becomes the scene of a homicide For both legal and moral reasons, employers must do whatever they can to protect their employees from violence and, to protect themselves from liability if violence should occur, these efforts should be documented in a Violence Warning and Prevention Plan ("Plan"). A minimally adequate Plan should have ten characteristics or elements:

1. The Plan Should Be in Writing

Because the Plan and its implementation may become evidence on which the employer would want to rely to demonstrate that it had taken all reasonable steps to avoid and prevent violence in the workplace, employers should put the Plan's purpose, elements and implementation steps in a written form that can be used in court. Recording the completion of the implementation steps is especially critical, because the only thing worse than having a Plan is having a Plan that is not implemented. While a Plan may be an effective shield against liability, it also can be a sword in the hands of a plaintiff's lawyer if the steps identified in the Plan as necessary are not taken. This risk, however, is no reason not to have a Plan. If an employer can think of dangers and preventive measures before an incident occurs, a plaintiff's lawyer will surely think of them after the event and assert that the employer "should have known."

2. Policies to Identify and Justify the Removal of a Potentially Dangerous Employee

There should be clear and calculated policies to neutralize the ability for a violent acts and indentify, neutralize and/or discharge high risk employees. At a minimum, these policies increase vigilance with respect to aberrant or suspicious behavior.

Clearly, firearms, explosives and cutting tools (other than small pocket knives) should not be permitted anywhere on the employer's property. Employees who are prone to emotional and violent behavior should not have access to any weapon while at work. Even if the owner of the firearm or knife is entirely responsible, the presence of the weapon in a place possibly accessible to a violence prone employee should dictate a policy with no exceptions and no tolerance.

To be effective, a weapon rule requires a companion policy that permits searches of personal belongings and storage areas of employees, including vehicles. The policy should state that the searches can be conducted without the necessity of a specific or precipitating cause.

Pre-employment drug/alcohol testing is now common for most employers. It should also be used during employment, at least when there is a reasonable suspicion of use/possession or following an accident resulting from employee negligence. Employees with alcohol and drug problems also have problems with self control, and these troubled people must be identified and assisted into rehabilitation programs or otherwise removed from the workplace.

In negligent retention cases, it is common to find that the perpetrator had said or done things that indicated a lack of respect for co-workers or a threat to the public. For this reason, an employer's discrimination and harassment policies must be tailored to include all forms of harassment, either as part of the general no discrimination, no harassment policy or as a stand-alone policy directed at violence prevention. Further, employers should not ignore angry or threatening statements/conduct just because the person's target is not an employee or the workplace in general.

3. Hiring Systems and Procedures to Identify Potentially Dangerous Applicants

Smart and thorough hiring practices may be time-consuming and boring. As a result, they usually are delegated to the least experienced human resource employee. Yet, a good hiring process is vital to any Plan. Applications must be carefully scrutinized, references actually contacted (and circumvented, if necessary, to get to the truth), social network sites checked (e.g., Facebook, YouTube), and criminal records reviewed. In addition, there also should be real interviews by someone who has been trained to spot potential problems and to judge applicants. Any suspicion must result in a no-hire decision.

4. Discipline Policies and Procedures That Are Not Unnecessarily Demeaning or Punitive

Many discipline systems are flawed in their design and, therefore, likely to be ignored or avoided by supervisors. As a result, opportunities to observe and correct behavior are missed. The most problematic flaws are those that demean employees by treating them as errant children. As a result, the policies fail in their primary purpose: the development and retention of productive employees.

Discipline systems should focus on the conduct, not the person, and should be corrective, not punitive. Punitive systems that rely on disciplinary unpaid suspensions as the final warning do little more than make people resentful and angry; they don't correct behavior. Even if the employee keeps her job, it probably is not due to, but in spite of, having lost pay and the scars of disrespect also will survive.

The disciplinary conference and discharge process also should be designed not to demean the employee. If an employee tends toward alienation and self-deprecation, an employer's validation of his feelings may be the match that sets the fire. In this regard, employers should consider a wider use of termination consultants in potentially difficult cases. These specialists can refocus the employee on the future and may neutralize many of the desires for revenge.

5. Supervisor Training

Supervisors are often an employer's first line of defense. They see employees every day and, if taught, will note changes in attitude and behavior that may indicate danger. These skills, like most for supervisors, need to be taught. The training should include the profiles of employees prone to violence, the means and methods of reporting questionable conduct, how to promote harmony between workers and how to resolve conflicts.

Finally, supervisors must learn the limits of their own abilities and authority. Supervisors are not professionals in dealing with volatile and dangerous employees. For this reason, the employer must build a support structure around the supervisors and teach them how to use it so that they are not forced to deal with complex and frightening situations alone.

6. Establish a Relationship with a Violence Expert

Employers should not rely on themselves to make critical judgments about whether a particular employee presents a threat to coworkers and, if so, what to do. Like supervisors, most managers are not experts in defusing and preventing potentially dangerous situations. Certainly, they are not capable of making the fine determinations with respect to whether an employee is a danger and must be removed from the workplace. Employers are also not qualified to devise and implement a course of action after a decision has been made. Even if an employee is found not to constitute an immediate danger, the fact remains that there was sufficient evidence to raise the question and this evidence may be sufficient to place special obligations on the employer to ensure that the decision was correct.

Fortunately, there are people and organizations that are qualified to help employers with these issues. Most of these experts are licensed mental health professionals who specialize in violence and violent personalities. It is important that employers establish a relationship with a violence expert at the time the Plan is being drafted to get their advice and to participate in the supervisory training. Having the expert intimately involved in the workplace before a difficult situation arises will make the expert better prepared to provide the right answer when needed.

At a minimum, the public and a jury will find it next to impossible to conclude that that an employer who relied on the advice of an expert acted unreasonably under all of the circumstances, even if the advice turned out to be tragically wrong.

Since many violent acts follow disciplinary or discharge events, employers also should make use of discharge counselors to help with high risk situations. These professionals are trained to redirect the anger and frustration of discharged employees into positive activities of putting their life back together and moving forward. Discharge counselors also permit the employer's decision makers to exit the office and conference room soon after delivering the bad news. By leaving the conference room, the responsible manager eliminates the opportunity for the employee to argue about the cause or justification for the decision and also removes the immediate target of employee anger. The discharge counselor has no ability to change the discharge decision and, therefore, is the best position to deal with the employee's outrage.

7. Employee Assistance Programs

Employee assistance programs serve several functions in a violence prevention program. First, they are resources for employees who may be troubled, thereby lessening the potential for violence. Second, they are people to whom supervisors can refer employees about whom they are concerned. Third, they are sources of support and advice for supervisors and managers who are dealing with an employee with violent tendencies or presentments. Finally, employee assistance programs may provide employer access to qualified mental health professionals who can.

8. Neutralize Structural Invitations for Violence

Some conditions invite opportunistic violent acts by strangers directed at employees. Parking or other areas where an employee can be attacked need to be brightly illuminated and, if necessary, any employee who enters those areas should be escorted. Surveillance cameras should be conspicuous so that their presence alone may be a deterrent, especially to a stranger looking for an opportunity to commit a violent act.

Special precautions must be taken for employees who work alone or in isolated areas to which strangers have access. Either additional employees should be added or security barriers erected to provide zones of safety.

9. Employee Communications

When dealing with violence, there is a fine line between being prepared and being an alarmist, causing more harm than good. While policies, such as those regarding weapons and belligerent conduct, need be published, how much cautionary information about violence should be in employee (as opposed to supervisory) training programs is less clear. Except under special circumstances, employee communications about the potential for violence probably should be limited to those that are included in policies about conduct (e.g., harassment) and about resources available for troubled employees (i.e., employee assistance programs). Clearly, the what and when of employee communications about violence should be included on the agenda for discussion with the violence expert/consultant.

10. Protocols for Special Situations or Conditions

Absolutely the wrong time to be deciding what to do is when you are actually faced with a potentially violent situation. Long before, in the relative calm of every-day life, employers should focus on what they will do in the event various scenarios become reality. All possibilities need to be examined to determine what, if any, action the employer will take and who will be responsible for implementing the steps indicated by the Plan. Answers need to be developed for such basic questions as: what should the manager do with a report of a possible threat? Whom should the manager call? Who should make the decision about whether something should be done?

The reasonableness of an action or decision not to act is most likely to be apparent to a jury and society in general if it is the implementation of a protocol developed by people whose abilities to make judgments are not compromised by the extreme tension of a real, live situation.

For example, the termination of employment is often the match that ignites the inner bomb of someone with violent tendencies. Many of the factors, such as the place, time, and people to be involved in discharge conferences, can be predetermined. For example, discharges should never take place in the office of the supervisor; employment terminations should be done in a conference room with the employer representative closest to the door so that her avenue of escape is not blocked. Other questions would include:

- should a termination of employment occur during or at the end of a work day;
- should the termination be on a Friday or on some other day of the week;
- should a discharge counselor be used and present and, if so, who;
- should there be other witnesses in the room and, if so, at what point will the employee feel overwhelmed, demeaned and threatened by being alone with numerous others he perceives as assembled for one purpose—observing his economic "capital punishment;"
- whether the employee should be confronted with the evidence of his wrongdoing in the presence of others or can that bit of drama be avoided?

* * *

There have been too many instances of fatalities due to violence in the workplace for employers to be able to plead surprise. The variables are pretty well known and most can be neutralized, limited or avoided altogether with advanced planning. A Violence Warning and Prevention Plan is the tool that may avoid a tragedy. A Plan also would avoid employer legal liability, because what is done or not done would be what a reasonable and prudent employer would do.

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Handling Terminations and Reductions in Force

By Marc B. Zimmerman

A former employee of a management client told the court-appointed mediator, “I have never felt as angry, embarrassed and sad as I did when I was fired.” Though the words are paraphrased, the sentiment is genuine—termination of employment is a devastating, even catastrophic, consequence, both economically and personally. It is an event that can cause individuals to react emotionally, rashly, aggressively and even uncharacteristically, particularly when replacement jobs are not easy to find. Therefore, whether resulting from economic necessity or discipline, employers should ensure that employee terminations are carefully planned, well-supported and tactfully performed to best defend against claims.

In most jurisdictions, employment is “at-will,” or generally terminable by employer or employee for any (or no) reason at all, without cause or prior notice. Common exceptions to “at-will” employment are employee terminations that violate civil rights laws (*e.g.*, based upon discrimination, harassment or retaliation) or those that violate employment contracts that require employment for a specific term or limit the circumstances in which a termination may occur.

Although employers are permitted to terminate employees “at-will,” they nonetheless may be called to task to defend against an employee claim that a termination was discriminatory or otherwise unlawful. Accordingly, it is critical for an employer to be able to support that an employment action is motivated by legitimate business reasons.

Employee Terminations—A Brief Review

A. Disciplinary Termination

A disciplinary termination is an involuntary end to employment resulting from an employer’s determination that an employee has, in some way (or ways), failed to satisfy an employer’s expectations. While appropriate disciplinary terminations can result from any number of factors, from unsatisfactory performance to workplace violence, all should share three common concepts: (1) the employer should have advised the employee that the employee conduct giving rise to the disciplinary termination was unacceptable and would result in termination; (2) the employer treats similarly situated employees engaging in similar conduct consistently and evenhandedly; and (3) the employer does not base any part of its decision to terminate on an employee’s membership in a protected classification or on any other unlawful basis.

It is advisable that employers create, distribute and enforce uniform policies and work rules for all employees to ensure employee understanding of employer expectations and consequences for falling short of such expectations. When engaging in discipline, up to and including termination of employment, an employer should uniformly and evenhandedly apply its policies and determine, by appropriate investigation and assessment, whether the punishment fits the violation. Generally, employers rely on the concept of “progressive discipline” to notify an employee of a failure to meet expectations and to alert the employee of the risks associated with future violations. Obviously, the progression may be dispensed with in favor of immediate action where the violation is sufficiently severe. In connection with any termination, however, employers must scrutinize their own employment decisions before they are made until they are satisfied that they can demonstrate the propriety of their decision if legally challenged.

B. Reductions in Force

In a difficult economic climate, employers increasingly are forced to rethink business considerations of growth, benefits and loyalty and instead focus on combining roles and cutting back on salaries and expenses to ensure continued success or, in many cases, survival. When even those efforts prove insufficient to meet budgetary demands, employers are forced to turn to non-disciplinary employee terminations and reductions in force (RIF) to address these issues. Employers also may recruit employees for RIF’s by offering economic incentives to volunteer for termination (*e.g.*, for those employees seeking to change careers or take early retirement). By employing such programs, employers may be able to effectuate desired staff reductions without the stigma associated with an involuntary termination.

The first step in preparing for a RIF (whether of a single employee or a group of employees) is determining, and articulating, a legitimate business reason for the decision, such as loss of business, department restructuring or plant closing. In so doing, employers should not assume that affected employees will agree with or accept the employer’s basis for a determination that leaves them without a job. Therefore, employers are well advised to be able to provide evidentiary support of their stated reason to combat employee claims that job eliminations packaged as a RIF were subterfuges for unlawful discrimination.

Once an employer articulates a legitimate reason for the RIF, it then must identify a decisional unit (a grouping of employees, *e.g.*, by department, job, or other business factor) to which the RIF is applicable and determine which employees in such unit will be selected for layoff. It is critical that employers spend significant time and effort to support both decisions of “how many” and “who” will be affected by a RIF. Specific reference to objective factors considered and evenhanded application of such factors to employees in the decisional unit often is the difference between an employer's ability and inability to withstand legal challenge by affected employees.

During this stage, employers should test their decisions from many angles. It is rarely sufficient, and always risky, to rely solely upon a "front-line" supervisor's recommendation alone without reviewing whether the employee(s) selected for the RIF actually fits the employer's legitimate selection criteria (e.g., seniority or productivity). In such instances, a selected employee may challenge the supervisor's recommendation as motivated by unlawful bias (even though the actual decision was made by a different individual), which could trigger "cat's paw" employer liability, discussed below. Additionally, a selected employee inevitably will be able to identify a comparator employee not chosen for layoff, and therefore, the more care taken by an employer to differentiate employees in a decisional unit both objectively and evenhandedly will pay off in the employer's ability to defend its decision against legal scrutiny.

Irrespective of the individual objective criteria used to select the individual employees affected by a RIF, employers always should be able to test the appropriateness of their "final list" by ensuring it can provide evidentiary support to answer the following questions: (1) are the remaining positions in the decisional unit affected by the RIF sufficient to satisfy the company's post-RIF goals? (2) did the company follow its own policies and practices in connection with the layoff? (3) does the number of employees selected for layoff in a decisional unit disproportionately affect employees of a particular protected classification? (4) are any of the employees selected on protected leave (e.g., medical or military); (5) have any of the employees selected engaged in protected conduct such as whistleblower, discrimination, harassment or wage/overtime complaints? and (6) will all the employees in the decisional unit selected for layoff be treated consistently in terms of applicable separation benefits?

In preparing for a RIF, employers must determine whether they are subject to the notification requirements of the federal Worker Adjustment and Retraining Notification Act[1] (WARN) or an applicable state counterpart. With very limited exceptions, WARN requires an employer that employs 100 or more employees to provide at least 60 calendar days advance written notice of a "plant closing"[2] or "mass layoff"[3] to affected employees, bargaining representatives and local government officials. If required WARN notices[4] are not provided (or if employees are not provided salary and benefits in lieu of WARN notice), employers may be subject to significant damages, including payment of full salary and benefits for the period for which notice was not provided, up to a maximum of 60 days, plus attorneys' fees. Some state WARN laws provide longer notice periods, a lower employee threshold and other protective provisions. For example, New York's WARN Act applies to employers who employ at least 50 full-time employees, covers employment loss of 25 employees, requires 90-day advance written notice of layoff and includes layoffs due to the relocation of all (or substantially all) employer operations to a different location 50 or more miles away.[5]

Awaiting Resolution on "Cat's Paw" Liability

Even where a decision maker himself exhibited no unlawful animus in connection with an employment decision, employers nonetheless must be cognizant of so-called "cat's paw" liability where an employer may be held liable based upon unlawful discriminatory intent of individuals who caused or influenced—but did not themselves ultimately make—an employment decision. Accordingly, employers plainly should be wary of blind reliance on the determination of a front-line supervisor to "rubber-stamp" an employment decision—particularly where the ultimate decision maker is in a separate department or higher on the chain of command with no direct connection to an affected employee.

On November 2, 2010, the U.S. Supreme Court heard oral argument in *Staub v. Proctor Hospital*,[6] a case involving a discharge allegedly in violation of the Uniformed Services Employment and Reemployment Rights Act (USERRA). The former employee argued that the discriminatory animus of a non-decision maker must be imputed to the decision maker where the former singularly influenced the latter and used that influence to cause an adverse employment action. The U.S. Court of Appeals for the Seventh Circuit reversed a jury verdict in the employee's favor, holding that prior to admitting evidence of animus by a non-decision maker, a trial court should determine whether a reasonable jury could find "singular influence on the evidence to be presented" before allowing the jury to entertain a cat's paw theory.[7] The court determined that even if the decision maker's independent investigation could have been more involved or "robust," it was enough to defeat cat's paw liability "that the decision maker 'is not wholly dependent on a single source of information' and conducts her 'own investigation into the facts relevant to the decision.'"[8]

Presumably, the Supreme Court will answer the question of whether, and to what extent, an unbiased decision maker will "own" an employment decision despite that a biased supervisor influenced the decision maker's decision. On a broader scale, however, this case is instructive to highlight the continued importance of an employer's thorough review and testing its employment decisions as a means to survive legal scrutiny.

After the Dust Settles—The Exit Interview and Release

A post-termination exit interview provides an employer a face-to-face opportunity to discuss business terms after the initial shock and emotions associated with the termination of employment. Such meetings are a means to reclaim company property in an employee's possession, provide the employee final compensation earned through the termination date; and explain any post-termination benefits to which the employee may be eligible. Although an employee often will take the opportunity to "vent," criticize or verbally attack a supervisor, a termination decision or the company itself (and may thereby provide an employer valuable information concerning potential claims), the individual conducting the interview should try to maintain a structured, informational process to discuss issues such as continuation coverage on a group health insurance plan, effects on employee benefit plans, post-employment benefits, unemployment insurance and restrictions on use of employer information. For those employers providing separation benefits, it also is an opportunity to provide the employee with a release seeking the waiver of claims against the employer and related persons and entities.

With employment litigation on the rise, more employers seek to eliminate the uncertainty of litigation in favor of a negotiated monetary settlement in return for a release. A properly drafted release provides the best defense to waivable claims arising up to the date of execution provided that it is supported by adequate consideration. The language should be clear and understandable so as to effectuate a knowing and voluntary waiver of all known and unknown claims.[9] An employee should have a reasonable opportunity to review the release,[10] and be advised to consult with counsel concerning the meaning and effect of the release. The release specifically should reference the types of claims released, and particularly, the employment-related statutes under which claims may arise. Although there are certain rights that may not be waived (*e.g.*, the right to file a charge with the U.S. Equal Employment Opportunity Commission[11] or other federal or state agencies), a proper release should restrict an individual's ability to gain or recover in any way in connection with claims that may be brought on the individual's behalf (*e.g.*, as a result of an agency or class resolution of such rights). Additionally, a release should contain an acknowledgment that an employer has paid all earned compensation and benefits through the termination date, and that the consideration provided is in excess of all earned compensation and benefits to protect against potential wage claims to the extent they are not waived.

Employer Recordkeeping—What to Retain and for How Long

Employer record retention serves two main goals: (1) compliance with applicable laws requiring retention of certain documents; and (2) to assist employers in defending against claims which can be refuted, in whole or in part, by information they maintain. It bears repeating that while even the best memories fade and the finest supervisors move on, personnel records remain.

The Equal Employment Opportunity Commission requires that all private employers covered by Title VII of the Civil Rights Act of 1964, as amended (Title VII), with more than 100 employees are required to file an annual Employer Information Report categorizing its workforce by sex, race and ethnicity.[12] The EEOC does not require that an employer maintain any specific personnel records of its employees for Title VII purposes, but an employer who does maintain such records concerning an employee (including requests for reasonable accommodation, job applications and other records having to do with hiring, promotion, demotion, transfer, layoff or termination, rates of pay or other terms of compensation) is required to maintain them for at least one year after the making of the record or the personnel action involved, whichever is later.[13] Where a charge of discrimination or agency action has been filed or brought against an employer under Title VII or the ADA, the employer is required to preserve all personnel records relevant to the charge or action (specifically including personnel or employment records relating to the aggrieved person and all other similarly situated employees or applicants) until final disposition of the charge or action.[14]

The EEOC requires that all employers subject to the Age Discrimination in Employment Act (ADEA)[15] make and keep for three years payroll (or other) records containing an employee's name, address, date of birth, occupation, rate of pay and amount earned each week.[16] ADEA regulations require that where an employer, in the regular course of its business, makes, obtains, or uses certain personnel or employment records (including applications, resumes, employment inquiries, records of promotion, demotion, transfer, selection for training, layoff, recall, or discharge) it must retain them for a period of one year from the date of the personnel action to which they relate.[17]

The Fair Labor Standards Act requires that employers must maintain for three years payroll records including each non-exempt employee's name, address, sex, occupation, hours worked each workweek, regular rate of pay, total wages paid and date paid.[18] The same general record and retention requirements apply to employers subject to the Equal Pay Act[19] and New York Labor Law.[20] An employer's failure to maintain such records risks its inability to refute an employee's wage claim and could subject it to substantial damages.

Conclusion

In the arena of employee terminations, the more things change, the more they remain the same. Despite the evolution in employment law, it still holds true that employers carefully must plan, review, question and scrutinize their employment decisions and motives in connection with such decisions. To neglect these central concepts is to risk the inability to refute a claim that an employment decision was unlawful.

Endnotes

1. 29 U.S.C. §§2101, *et seq*.
2. The permanent or temporary shutdown of a single site of employment, or one or more facilities or operating units within a single site of employment, resulting in an employment loss during any 30-day period at the single site of employment for 50 or more full-time employees. *See* 20 C.F.R. §639.3(b).
3. A reduction in force not resulting from a plant closing that results in an employment loss at a single site of employment during any 30-day period for at least 33 percent (but at least 50) of the active, full-time employees; or for 500 or more full-time employees. *See* 20 C.F.R. §639.3(c).
4. WARN notices must set forth certain specific information, including identifying the employment site where the plant closing or mass layoff will occur; a company representative to provide further information; job titles of affected positions and names of employees currently holding affected jobs; the expected date of the first termination and anticipated schedule of terminations; whether the layoffs will be temporary or permanent; whether bumping rights (to displace other, *e.g.*, less senior, employees) exist; and each union and chief elected official thereof representing affected employees. *See* 20 C.F.R. §639.7.
5. *See* N.Y. Lab. L. §§860, *et seq*.
6. U.S. Sup. Ct. No. 09-400, *cert. granted,* 130 S.Ct. 2089 (2010).
7. *Staub v. Proctor Hosp.*, 560 F.3d 647, 658 (7th Cir. 2009), *cert. denied*, 130 S. Ct. 2089 (2010).
8. *Id.* at 659.
9. Releases of all claims under certain state statutes may specifically require language waiver of unknown claims. *See*, *e.g.*, Cal. Civ. Code §1542 (“A general release does not extend to claims which the creditor does not know or suspect to exist in his or her favor at the time of executing the release, which if known by him or her must have materially affected his or her settlement with the debtor.”).
10. The Older Workers Benefit Protection Act requires that employees 40 years of age or older receive at least 21 days (45 days where a layoff is in connection with a termination plan or program offered to more than one employee) to consider the agreement (the employee may waive that requirement and sign earlier) and 7 days to revoke the release after the employee has executed it. *See* 29 U.S.C. §§626(f)(1)(F) and (G).
11. *See* Enforcement Guidance on non-waivable employee rights under Equal Employment Opportunity Commission (EEOC) enforced statutes, EEOC Notice 915.002, at III(C) (April 10, 1997) (“while a private agreement can eliminate an individual’s right to personal recovery, it cannot interfere with EEOC’s right to enforce Title VII, the EPA, the ADA, or the ADEA by seeking relief that will benefit the public and any victims of an employer’s unlawful practices who have not validly waived their claims.”).
12. *See* 29 C.F.R. §1602.7.
13. *See* 29 C.F.R. §1602.14. The same is required under the Americans With Disabilities Act. *See* 42 U.S.C. §12117(a).
14. *Id*.
15. Employers engaged in an industry affecting commerce having 20 or more employees for more than 20 calendar weeks during the current or previous calendar year. *See* 29 U.S.C. §630(b).
16. *See* 29 C.F.R. §1627.3.
17. *Id.*
18. *See* 29 C.F.R. §516.2(a).
19. *See* 29 C.F.R. §1620.32(a).
20. *See* N.Y. Lab. L. 195(4).

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A Guide to Dealing with Workplace Substance Abuse

By Sharon P. Stiller and Scott R. Simpson

Scenario 1:

Having washed out of films, Lindsay applies to become Don's new assistant (Don is notorious within advertising for his checkered history of ex-assistants). Lindsay gets the job and manages to meet the requirements for a while.

Lindsay begins to show up to work late. This pattern worsens, as Lindsay frequently disappears without anyone knowing her whereabouts.

Due to Lindsay's much publicized bouts of drug abuse and treatment, Don knew of Lindsay's issues. In fact, Lindsay had "tweeted" about dealing with her addiction. Don's attorneys told him that he could not refuse to hire Lindsay because she had a history of substance abuse. Don does not want to run afoul of any disability laws. Don wonders whether he can ask Lindsay if her absences are caused by a relapse. What should he do?

Is the Substance Abuser Protected Under Federal and State Disability Laws?

The federal Americans with Disabilities Act (ADA) prohibits covered employers from discriminating against a qualified individual with a disability in most aspects of the employment relationship.[1] To be considered disabled under the ADA, an individual must (1) have a physical or mental impairment that substantially limits one or more major life activities, (2) a record of such impairment, or (3) be regarded as having such an impairment.[2]

That an employee is a drug addict or alcoholic does not mean the employee is automatically considered disabled. The addiction must substantially limit one or more major life activities.[3] Further, the ADA provides that an employee *currently* engaged in illegal drug use is not considered disabled when an employer takes action against the employee on the basis of that drug use.[4] Because drug testing is not considered to be medical testing, disclosing that a terminated employee failed a drug test is not disability-related harassment.[5]

Beyond the ADA, there are other federal and state statutes that impact substance abusers and testing in the workplace. Section 504 of the Rehabilitation Act of 1973, the New York Human Rights Law (the "State HRL") and the New York City Human Rights Law (the "City HRL") all prohibit employer discrimination based on disability.[6] In general, all three statutes are interpreted similarly to the ADA.[7] Some of the subtle differences, however, can be vitally important.[8] For example, both the Second Circuit and the New York Court of Appeals have recognized that the term "disability" is broader under the State HRL.[9] Therefore, a substance abuser can be disabled under the State HRL "if his or her impairment is demonstrable by medically accepted techniques; it is not required that the impairment substantially limit that individual's normal activities."[10]

Even assuming a substance abuser is deemed disabled, the employer can still hold the employee to the same standards as other employees.[11] For example, an alcoholic who is chronically late to work can be fired for tardiness, even if the lateness stems from the disease.[12]

This last point brings us back to our hypothetical. Don's attorneys were correct that he could not refuse to hire Lindsay because she is a former substance abuser. However, there is nothing illegal about insisting that Lindsay meet the attendance requirements of her position. If Lindsay admits that her attendance problems were caused by current drug use, Don may terminate her because the ADA and other disability laws do not protect current drug users. But, if Lindsay claims she is rehabilitating and needs some time off to attend treatment, Don must accommodate the reasonable request if Lindsay will be able to perform her job with the accommodation.

Drug and Alcohol Testing: Is It Mandatory, Permissible or Even Helpful?

Scenario 2:

When Lindsay tells Don she needs a reasonable accommodation to allow her treatment to continue, Don is skeptical and wonders if he can require Lindsay to take a drug test to prove she is no longer using. Don's firm does not have a drug testing policy.

The ADA explicitly states that it is not to be interpreted to encourage, prohibit or authorize drug tests by employers.[13] It is therefore generally permissible for an employer to drug test both prospective and current employees and to take disciplinary action against an employee who fails her drug test.

The rules for alcohol testing are slightly different than those for drug testing. Testing for the presence of alcohol is considered as a medical test under the ADA.[14] Therefore, before an employment offer is made, employers cannot test prospective employees for alcohol.[15] Post-offer, the ADA prohibits the medical testing of employees unless the testing is shown to be job-related and consistent with business necessity.[16]

Interestingly, the Second Circuit has held that the ADA is not violated by testing an employee with a history of substance abuse more frequently than an employee with no such history. In *Buckley v. Consolidated Edison Co. of N.Y.*, Buckley was identified as a substance abuser and was required to submit to random drug and alcohol testing approximately once every 25 days.[17] Buckley suffered from a condition colloquially referred to as "shy bladder syndrome," causing an inability to urinate, particularly in public or on command. Buckley was unable to produce a urine sample in the time allotted by his employer, and was terminated.

The Second Circuit found that the plain text of the ADA allows the more frequent testing of substance abusers.

The plaintiff in *Buckley* did not contend that shy bladder syndrome *itself* was a disability, and the courts have divided about the issue. A Tennessee federal district court held that it was premature to decide on the pleadings whether shy bladder syndrome is a disability under the ADA.[18] However, in granting summary judgment for the defendant, a Wisconsin federal district court found that shy bladder syndrome was not a disability.[19]

In 2008, Congress expanded the definition of "major life activities" by listing "the operation of a major bodily function, including but not limited to functions of the… bladder."[20] Given this new definition, a plaintiff could argue that shy bladder syndrome substantially limits the functioning of the bladder within the meaning of the ADA, therefore warranting reasonable accommodation.

Dealing with Substance Abusers in the Workplace

The first step toward effectively dealing with substance abusers in the workplace is to draft a policy providing that any employee currently using, possessing or under the influence of illegal drugs or alcohol at work is subject to discipline. In most situations, problems caused by substance abuse can be addressed through focusing on performance and performance reviews, without ascertaining the root cause of the poor performance. By dealing only with employee conduct, the employer avoids concerns about improperly labeling an employee as disabled or about failure to accommodate.

Employers may also consider implementing a universally enforced drug and/or alcohol testing policy. There is no legal requirement or prohibition on workplace drug or alcohol testing in New York. Due to the expense and employee-perceived intrusion associated with workplace drug or alcohol testing, adopting a testing policy may be unnecessary, except for regulated industries (e.g., trucking), certification purposes or in safety-sensitive industries.

Where employee mistakes caused by substance abuse present dangerous situations for the employee and/or co-workers, it is cost-effective and has a deterrent impact to implement a carefully crafted testing policy. Such a policy may require testing randomly, after any workplace accident or when a supervisor reasonably believes an employee is under the influence during work hours. The testing policy should be communicated to all employees, and each employee should execute an acknowledgment of receipt.

A drug or alcohol testing policy should not require an employee's termination upon testing positive. An employer does not want to be in a position where a star employee must be terminated as a result of an isolated positive test. Also, any testing policy must specify that a negative test does not preclude disciplining under other policies (e.g., the employee conduct policy). This language avoids the implication that an employee involved in an industrial accident, and who has a history of such accidents, will keep the job if test results are negative.

We stress that any conduct or substance policy must exist not only in form but in daily practice. Any uneven or selective enforcement of a substance abuse policy can subject the employer to a disparate treatment claim. As stated above, the Second Circuit has sanctioned testing substance abusers (even those not currently using substances) more frequently than non-substance abusers, but an employer's testing policy should make clear that the employer reserves that right.

Closing the loop on the saga of Don and Lindsay, we suggest that Don warn Lindsay about her performance, and inform her that continued unexcused absences will result in termination. If Lindsay asks for time off for rehabilitation, it should be granted.[21] We would not recommend that Don ask Lindsay to submit to a drug test, especially without a testing policy. Lindsay's absenteeism can be addressed through Don's employee conduct policy without resort to drug testing.

Endnotes

1. *See* 42 U.S.C. § 12112(a), 12111(5)(A) (defining "employer").
2. 42 U.S.C. § 12102(1).
3. *Reg'l Econ. Cmty. Action Program, Inc. v. City of Middletown*, 294 F.3d 35, 47 (2d Cir. 2002); *Skinner v. City of Amsterdam*, __ F.Supp.2d __, 2010 WL 1223032, at *6 (S.D.N.Y. Mar. 30, 2010). *See also EEOC v. J.B. Hunt Transport, Inc.*, 321 F.3d 69, 75-78 (2d Cir. 2003) (no ADA violation where trucking company refused to hire individuals taking prescription drugs that could impair driving ability because the company only viewed these individuals as being unfit for a specific job rather than a broad classification of jobs).
4. 42 U.S.C. § 12114(a).
5. *Skinner*, 2010 WL 1223032, at *14.
6. 29 U.S.C. § 794(a); N.Y. Executive Law § 296(1)(a); N.Y.C. Admin. Code § 8-107(1)(a).
7. *Henrietta D. v. Bloomberg*, 331 F.3d 261, 272 (2d Cir. 2003) (the ADA and the Rehabilitation Act will be applied similarly unless a statute's specific terms dictate differently); *Robertson v. Amtrak/*

Nat'l R.R. Passenger Corp., 400 F.Supp.2d 612, 623 (S.D.N.Y. 2005) (disability claims brought pursuant to the Rehabilitation Act, the State HRL and the City HRL are construed similarly to ADA claims); *State Div. of Human Rights v. Xerox Corp.*, 65 N.Y.2d 213, 218-19, 491 N.Y.S.2d 106, 109 (1985).

8. *See* 29 U.S.C. § 794(a) (Rehabilitation Act only applicable to employers receiving federal funding); Exec. Law § 292(5) (defining an "employer" as having at least four employees); N.Y.C. Admin. Code. § 8-102(5) (same).

9. *Batac v. Pavarini Const. Co., Inc.*, 216 Fed. Appx. 58, 61 (2d Cir. 2007); *Treglia v. Town of Manlius*, 313 F.3d 713, 723-24 (2d Cir. 2002).

10. *Reeves v. Johnson Controls World Servs. Inc.*, 140 F.3d 144, 155 (2d Cir. 1998) (internal quotation marks omitted). *See also* Exec. Law § 292(21).

11. 42 U.S.C. § 12114(c)(4).

12. *Vandenbroek v. PSEG Power CT LLC*, 356 Fed. Appx. 457, 460 (2d Cir. 2009) (an alcoholic with chronic attendance problems was not otherwise qualified to perform the essential functions of his job); *Daddazio v. Katherine Gibbs Sch., Inc.*, No. 98 Civ. 6861, 1999 WL 228344, at *5 (S.D.N.Y. Apr. 20, 1999) (noting that regular attendance is an essential function of every job), *aff'd* 205 F.3d 1322 (2d Cir. 2000*). But see Teahan v. Metro-North Commuter R.R. Co.*, 951 F.2d 511, 515-16 (2d Cir. 1991) (under the Rehabilitation Act, an employee is fired because of her disability when the decision is based on conduct caused by alcoholism). However, even in *Teahan*, the Second Circuit thought that an employee who frequently failed to come to work as a result of alcoholism may not be "otherwise qualified" for his job. *Id*. at 515, 520-21.

13. 42 U.S.C. § 12114(d)(2). *See also* 42 U.S.C. § 12114(b).

14. Equal Employment Opportunity Commission, *Enforcement Guidance: Disability-Related Inquiries and Medical Examinations of Employees under the Americans with Disabilities Act*, *at* http://www.eeoc.gov/policy/docs/guidance-inquiries.html (last viewed Sept. 21, 2010).

15. 42 U.S.C. § 12112(d)(2)(A); Equal Employment Opportunity Commission, *ADA Enforcement Guidance: Preemployment Disability-Related Questions and Medical Examinations* 16, *at* http://www.eeoc.gov/policy/docs/medfin5.pdf (last viewed Sept. 21, 2010).

16. 42 U.S.C. § 12112(d)(4)(A).

17. 155 F.3d 150 (2d Cir. 1998).

18. *Melman v. Metro. Gov't of Nashville & Davidson County*, No. 3:08-cv-1205, 2009 WL 2027120, at *3 (M.D. Tenn. July 9, 2009).

19. *Balistreri v. Express Drug Screening, LLC*, No. 04-C-0989, 2008 WL 906236, at *5 (E.D. Wis. Mar. 31, 2008).

20. 42 U.S.C. § 12102(2)(B).

21. In addition to the disability statutes, Lindsay's request for time off for the treatment of her drug addiction may implicate the Family and Medical Leave Act (FMLA). *See* 29 U.S.C. § 2612(a)(1)(D); 29 C.F.R. § 825.119(a).

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Busting Myths About Overtime Law: Avoiding Wage and Hour Claims

By Joel J. Greenwald

Overtime wages can be a major part of any organization's staffing expense. The only thing more expensive than paying overtime is *not* paying overtime when it's due—since if employees prevail on an overtime claim, they can receive double damages plus attorneys' fees. In addition, governmental agencies investigating overtime claims can also impose fines on overtime violators. In New York, the statute of limitations for wage claims is six years.

In my practice, which consists of advising and representing management regarding employment law issues, nothing is hotter than overtime-based audits and lawsuits. As businesses cut back—on jobs, on raises, on hours, on benefits—employees often feel hurt and betrayed. Those feelings, coupled with economic stress, lead many to filing litigation against their employers or former employers to recoup their perceived losses.

However, the economy is only part of the reason for this increased litigation. I often find that employers make basic mistakes that leave them open to legal action. There's a wealth of misinformation and myths out there about employment law—especially regarding wages, hours, and overtime entitlements—that lead to companies creating unnecessary liability.

Fortunately, with a little knowledge, you can avoid much potential overtime liability. Most of the overtime traps that employers fall into can be avoided by busting some common overtime misperceptions. When in doubt, you should bring in experienced employment counsel to advise or represent you, but the following are eight common overtime myths that often trip up employers.

Overtime Myth # 1: If Employees Don't Work More Than 80 Hours in a Two-Week Pay Period, They're Not Owed Overtime Pay

Since payroll cycles are generally based on 80 hours worked across two weeks, it's tempting—and common—to think that same cycle applies to overtime. As long as employees don't work more than 80 hours in the pay period, companies think they are not owed overtime pay.

Unfortunately, that's not the law. Under federal law, any nonexempt employee who works more than 40 hours in a single workweek must be paid overtime for all hours worked past 40 in that week. For example, Pat worked 45 hours in Week 1 of a two-week pay period and 33 hours in Week 2. Even though week 2 is under 40, all five hours over 40 in Week 1 must be paid at an overtime rate.

Overtime Myth # 2: Salaried Staff Don't Receive Overtime Pay

It's common for people to use "salaried" as a proxy or shorthand for "overtime exempt." However, the belief that if someone is paid on a salary basis they don't get overtime is not necessarily true. Being paid on a salary basis is only one requirement to be exempt from the overtime requirements. It's not the whole test. To be exempt from overtime, an employee must meet all the criteria, which revolve principally around the employee's duties. So as counterintuitive as it may seem, salaried staff *can* earn overtime. You should compare your employee's job responsibilities to the overtime exemption tests (which you can find at www.dol.gov) to see whether the employee is owed overtime pay.

Overtime Myth # 3: Managers Don't Receive Overtime

It often seems odd to pay a "manager" overtime. However, whether a manager is exempt for overtime purposes has nothing to do with what it says on his or her business card. The test for the executive exemption is very specific, and if an employee who "manages" other people doesn't meet its criteria, the title is irrelevant. The key criterion is whether the manager manages at least two full-time employees or FTE's (full-time equivalents).

It's not the only requirement, however. To fit under the "executive exemption" a manager must:

- Be compensated on a salary basis at a rate not less than $455.00 per week (states may set higher minimums);
- Have a duty managing the enterprise, or a customarily recognized department or subdivision of the enterprise; and
- Have the authority to hire or fire other employees, or the manager's suggestions and recommendations as to the hiring, firing, or other employee change of status must be given particular weight.

Since titles are cheaper to give than raises—and can help an employee deal with people outside the organization—it's not uncommon to have "managers" who don't actually manage anyone. (For example, there are marketing "managers" or account "managers.") These managers may also be entitled to overtime pay, or these managers who manage an area instead of people may be exempt under the "administrative exemption" test if they:

- Are compensated on a salary basis at a rate not less than $455.00 per week;
- Have a primary duty performing office or non-manual work directly related to the management or general business operations of the employer or the employer's customers; and
- Exercise discretion and independent judgment with respect to matters of significance.

The most important thing to remember is that to be exempt from the overtime pay requirements, an employee's title is not dispositive. The employee *must* meet one or more of the Fair Labor Standards Act exemptions. If the employee doesn't, he or she is eligible for overtime. Employers must make sure that all their "managers" qualify for an exemption before failing to pay them overtime.

Overtime Myth # 4: Commissioned Sales People Don't Get Overtime

Surely if someone is a commissioned sales person, he or she doesn't receive overtime? After all, their reward for working harder or longer is a (presumably) larger commission from making more sales. Unfortunately, as logical as that may be, it's not the law. Only outside commissioned sales representatives (and other limited exceptions) don't receive overtime. Otherwise, even if sales people receive a commission, they are also probably eligible for overtime.

According to the Department of Labor, for an outside commissioned sales representative to not receive overtime, the employee must:

- Make sales, or obtain orders or contracts for services or for the use of facilities for which a consideration will be paid by the client or customer; and
- Be customarily and regularly engaged away from the employer's place of business.

Thus, there are a lot of employees who *don't* qualify for this exemption, including: inside telesales staff; customer service or account representatives who service customers or accounts but don't primarily sell or originate new business, and most, if not all, marketing personnel.

Companies may try to get around this by making their sales staff independent contractors. And *if* the employees are truly independent contractors, that could work. But, the question shifts now to whether they are, in fact, independent contractors. As in so many areas of the law, what you call an employee doesn't matter—all that counts is the reality of their relationship with the employer. The proper classification of workers as employees or independent contractors is a topic unto itself, but a quick rule of thumb—if the worker is not "independent" in terms of being able to control his or her own hours, place of working, or how he or she does the job, or is not "independent" financially of the employer, then he or she is probably *not* an independent contractor.

Overtime Myth # 5: You Can Offer Comp Time Instead of Overtime

Comp time, even if offered at the rate of 1½ hours for each hour of "overtime" worked, cannot be substituted for overtime wages, even though this seems equivalent.

The law doesn't allow private employers to compensate nonexempt employees with time, not money, for working more than 40 hours in a workweek. Instead, under federal and New York law, nonexempt private employees must be paid overtime pay. If an employee is eligible for overtime, comp time is not an acceptable substitute.

Overtime Myth # 6: You Don't Need to Pay Overtime if an Employee Agrees to Not Receive It

Employment at will and the freedom to contract would seem to mean that an employee is free to contract away overtime pay. In fact, many employers have employees agree to not be paid overtime.

Unfortunately, the law doesn't allow employees to do this. Under the law, the right to overtime can *never* be given up by agreement or contract. Freedom to contract stops somewhere short of contracting away overtime rights.

(As a practical matter: if you have a budget cap but also expect that the job will involve regular overtime, reduce the base. Set it at a level that provides the employee with the desired compensation after working the normally expected hours.)

Overtime Myth # 7: There's Never Overtime for On-Call Time, or Work Done Before or After Normal Working Hours, or Work Done at Home

Work is work is work. Under the wage and hour laws, nonexempt workers need to be paid for *all* work done, no matter where (onsite or off) or when (during shift or after) it's done. If a nonexempt worker works more than 40 hours in a work week, even if part of it is after the normal shift or from home, the employee is entitled to overtime.

What about pay and overtime for on-call time? The answer is a more nuanced "it depends." While the full test for when on-call time is work time is complex, the basic distinction is between—

- Simply being available to be called (or called in), when the employee is otherwise free to go or do whatever he or she wants, while waiting for a call that may never come; and

- Having to wait in a ready room, or stay within a certain amount of response time (*e.g.*, fifteen minutes) of work, with restrictions on activities.

In the former case, unless the workers are actually called, they didn't work— they just carried a cell phone. However, in the latter case, they've been restricted in what they can do or where they can go for the employer's benefit. In that case, that restriction may mean that the employees are working—and earning overtime, as applicable.

Overtime Myth # 8: There's Never Overtime for Working More Than 8 Hours in a Day, or for Working Weekends, as Long as the Employee Worked 40 or Less Hours Total in the Week

Under federal law, overtime is only owed when a nonexempt worker works more than 40 hours in a single workweek. It doesn't matter whether the employee worked 12 hours in a day, the graveyard shift, or weekends.

However, that's federal law—there's also state law to consider. States can be more generous to workers than federal law is and they can offer overtime in more situations than federal law. So, for example, California requires that overtime be paid whenever a nonexempt worker works more than 8 hours in a day. If there's a nonexempt worker in California who only works 30 hours in week—but 11 of them are on Monday—the worker needs to be paid for three hours at time-and-a-half.

It's vital to *always* check state law for overtime obligations.

It's also important to note that overtime is earned for *working* more than 40 hours in a week. Paid leave or paid time off, such as paid holidays, vacation, sick, or personal days, don't count towards overtime. You don't need to pay employees overtime wages when they use paid time off, unless they actually *worked* for more than 40 hours in that week.

Conclusion: A Little Knowledge Goes a Long Way

Employment law, especially wage and hour topics, can be very complex, such as whether and to what extent employees need to be compensated for "on call" time. However, most of the time, if a business gets in trouble and faces a lawsuit or an agency enforcement action, it's for something basic—such as not paying overtime to "managers" who don't manage, or trying to avoid paying overtime period. If businesses avoid the more basic overtime errors, they'll often avoid the bulk of overtime liability.

DISCLAIMER: The foregoing is a summary of the laws discussed above for the purpose of providing a general overview of these laws. These materials are not meant, nor should they be construed, to provide information that is specific to any law(s). The above is not legal advice and you should consult with counsel concerning the applicability of any law to your particular situation.

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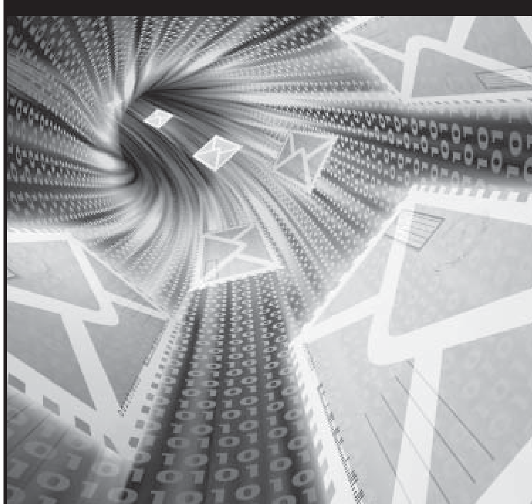

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Launching Employment Operations in a New Overseas Jurisdiction: A Guide to the Employment Law Issues

By Donald C. Dowling, Jr.

A multinational branching out internationally almost always employs people (or at least contracts with services providers) in one or more new countries abroad. Done right, this process is always complex, and can be confounding. Whether a domestic U.S. business explores how to set up its first-ever foreign outpost in Toronto or a multinational conglomerate already operating across 51 countries plans to open a new facility in its 52nd, going into a new country—and identifying and following its local "rules of the road" as to human resources and employment law compliance—is always a challenge.

This article is a toolkit for a business or non-profit employer branching its operations out into some new country and planning to employ (or contract with) its first-ever staff engaged in that jurisdiction. We focus on the scenario of tiptoeing into a new jurisdiction with only one or a few employees or contractors, although much of our discussion also applies to a business going "all in" and opening a full-service (large staff) facility in a new country. The discussion breaks into two parts: "floating" employees working in overseas "permanent establishments" (how to set up an employer presence abroad, with a focus on small start-ups without a lot of in-country infrastructure), and a checklist of issues for launching HR operations in a new country (what human resources issues to address in a new overseas employer operation).

Part 1: "Floating" Employees Working in Overseas "Permanent Establishments"

Multinationals entering a new foreign market by jumping in with both feet, employing lots of staff in some new local office, plant or operation, tend to invest the resources necessary to enter the new market without taking shortcuts. They tend to spend the time and money to get it right, setting up a local representative office, branch, or subsidiary, getting it fully licensed, and complying with local corporate laws, tax laws, employment laws and immigration laws. Entering a new market in this way—"all in," formally establishing a registered commercial presence and complying with all local laws, is always a best practice. The reverse—violating applicable law—is *never* a best practice.

But what about the employer tiptoeing into a new overseas market who plans a tiny presence operation with just one or two local in-country employees? What about the employer that will operate only temporarily in some foreign country? What about the non-profit executing some limited, tight-budget contract in the new country? And what about when an employee moves abroad for personal reasons, asking to work remotely from a new home in a country where the employer otherwise does not operate? Must all these employers always take the same time-consuming and expensive "all-in" approach as the business launching a major in-country operation?

Not surprisingly, many businesses and non-profits taking baby steps into a new overseas jurisdiction shy away from the "all-in" model. They seem to prefer placing an employee into a target country without building all the infrastructure of a formal licensed and registered in country employer entity. We might call these arrangements "floating" employment, because the in-country "floating" employee is not anchored to any local employer-entity infrastructure.

These days there seems to be a marked upswing in these floating employee arrangements. And from a practical perspective this trend should come as no surprise: Technology facilitates the approach. In the old days (say, up to the 1980s), a multinational's in-country local representative would have needed dedicated office space, a secretary and other support staff. But today's floating employee can work efficiently from home with little physical infrastructure beyond a computer, cell phone, express courier delivery and perhaps video conference software.

Technology may facilitate floating employee arrangements, but *legal* issues frustrate them. And the very same advances in technology allow tougher enforcement by local regulators. Floating employee arrangements are suspect and risky, because they often violate local laws—especially where the non-resident employer entity is deemed to have an unregistered so-called "permanent establishment" (local business presence subject to being taxed).

Multinationals' overseas employment operations inevitably raise structuring issues: *How do we employ someone in a foreign country? Which entity should be the employer? How do we get comfortable that the arrangement complies with local law?* Generally the best advice is to avoid floating employee arrangements and get a local employer entity registered in each country where the employer employs people. But some employers see this full-registration approach as impossible. Fortunately, in certain circumstances there *are* legally compliant strategies for engaging overseas floating employees—strategies such as "leasing" an employee from an up-and-running local employer or engaging a legitimate independent contractor. But implementing a legally compliant strategy in this context requires addressing a number of disparate issues. Floating employee arrangements raise legal traps under local host country laws, including: commercial registration requirements, corporate income tax requirements, labor/employment law (payroll, leasing/"secondment" and independent contractor issues) and immigration law. We address each in turn.

Commercial Registration

When a multinational has an employee who makes short, intermittent business visits into a country without establishing a local residence, without signing contracts and without generating in-country revenue, the employer may not cross the jurisdiction's local "doing business" threshold and probably will not be considered a local "permanent establishment." But once a multinational engages staff based in a foreign country to develop the local market—or even just to work on local soil for the *worker's own* convenience—then the analysis gets complex. And it differs from country to country.

An employer that crosses a jurisdiction's local "doing business" threshold and is deemed under local law to be transacting business locally must generally register in the country's local "Companies Registry," "Commercial Registry," or other local equivalent to a U.S. state's secretary of state corporate registration office. Usually this registration means fulfilling the requirements for some category of locally recognized corporate registration status. In the Philippines, for example, an incoming foreign corporation that wants to do business locally has three registration options: representative office, branch, or wholly owned (locally incorporated) subsidiary. In countries such as Ethiopia, a company will need both to register locally and also apply for a "business license."

Our question becomes: *When does an employer operating abroad cross the "permanent establishment" threshold and become obligated to get registered in the local companies registry?* The answer differs by locale. Malawi, for example, requires only those businesses with a "local established place of business" to register—but Malawi uses a broad definition for "place of business" that can include, for example, even a government department office that hosts a local company employee. Mexico looks to whether the business has a local physical presence *or* whether the business has local agents with power of attorney. By contrast, Qatar requires every natural or "juristic person" to register before "engaging in commerce"—but Qatari commercial registration law is murky as to what "engaging in commerce" means. Other countries, like Syria, set out illustrative lists of factors that determine when a foreign business triggers the local registration requirement. A Syrian decree sets out five factors:

1. hiring workers paid by the employer (our "floating" employee situation)
2. buying or renting local real estate in employer's name
3. opening a local bank account in employer's name
4. listing the employer in a local telephone directory
5. subscribing to a post office box (in Syrian parlance a "telegraph address") in the employer's name

Once an employer's overseas presence triggers the local country's threshold for commercial registration, the question becomes: *What must the employer file?* Registration requirements differ from country to country and the requirements differ depending on the corporate status selected (representative office, branch, subsidiary). Requirements here can include:

- providing a local address
- naming a local-resident agent (and sometimes, such as for a branch in Malawi, even naming an entire board of directors—notwithstanding that a local branch technically is not a separate entity)
- empowering a local authorized agent via an apostiled and translated power of attorney
- registering with local tax, social security and other government authorities
- opening a local bank account with a minimum required paid-in capital
- issuing a bond locally in favor of third party claimants
- making industry-specific filings (for example, special authorizations are required for engineering firms in Brazil, news organizations in Vietnam and retail sales operations in the Philippines)

This raises the question of compliance: *What happens if an overseas-based employer violates these registration rules and operates an unregistered local "permanent establishment"?* In countries such as Spain and Mexico, corporate registrations may be seen as largely notarial acts and a failure to register may mean only civil, tax and employment exposure. But in other countries local corporate registry officials have police power to investigate, charge and fine a foreign business that flouts local registration laws. The Democratic Republic of the Congo, for example, can seize assets and ban an unregistered business and its agents from operating in-country. The Philippines can sentence business people who sell products locally without registering under a local "retail trade" law to 6–8 years in prison.

Violations of corporate registration requirements are likely to come to light when a local employee quits or gets fired. Violations also get rooted out as advances in technology help enforcers scrutinize "floating" employee arrangements ever more closely. Non-compliance threatens financial costs that run higher than mere fines and lawsuits, in that failing to register impedes acts that require proof of commercial registrations—renting office space, opening a bank account, importing goods through customs, selling to a government entity. In Norway, for example, a business is virtually paralyzed without a registration number from the Norwegian Register of Business Enterprises. And an employer's failure to get local commercial registrations can cascade into violations of other local laws, be they corporate tax requirements, employment rules, or immigration mandates. Each is discussed below.

Corporate Tax

Outside the few "tax haven" jurisdictions such as Bahrain and UAE that impose no corporate income tax, any enterprise operating somewhere through a "floating" employee—even an employer not generating profits from the local market and even an organization registered in its home country as a non-profit—exposes itself to filing obligations and local tax liability under local corporate tax laws. In short, a local "permanent establishment" (foreign business operating locally) will have to file a local corporate tax return. Whether any corporate tax *payment* is actually due locally will be a fairly straightforward analysis if the local host country and the multinational's home country have executed a tax treaty for avoiding double taxation. Where there is no treaty, local income tax laws will apply, with their local definitions of taxable income and their domestic principles of tax liability.

When a local floating employee triggers a corporate tax-filing requirement, the unregistered employer may argue that its local representative plays a non-revenue-generating role and triggers no permanent establishment. Whether this argument prevails turns on the facts and definitions under local corporate tax law. That said, if local (in-country) customers buy products or services or pay bills through the floating employee, the employer may have a tough time arguing its in-country operations generate no taxable local revenue—especially, but not necessarily, if the local employee has agency authority to bind the employer.

Labor/Employment Law (Including Payroll, "Secondments," Independent Contractors)

Countries everywhere extensively regulate employment relationships, imposing rules on such topics as:

- Employment contracts/fixed term agreements/probation periods
- Compensation (wages/overtime/bonuses/profit-sharing)
- Personal income tax withholdings/social security/social insurance contributions/other social funds
- Part time/temporary work
- Caps on work hours/overtime pay/wage-hour rules
- Vacation/public holidays
- Health/safety
- Firings/severance pay

Local employment laws will generally reach a single employee local start-up operation of a foreign-owned employer—a floating employee—even if employer and employee had agreed on a choice-of-law clause that purports to apply the law of the employer's headquarters country. Local employment protection laws almost invariably reach a multinational's in-country employees by force of public policy regardless of employee citizenship and regardless of a choice-of-foreign-law clause in an employment agreement.

Native local employers in an overseas market may be predisposed to comply with local employment laws, but an overseas-based employer new-to-market with no local infrastructure will face employment-law compliance challenges, for two reasons: (1) full compliance with local employment laws is difficult when the local rules are not readily available and are foreign to the employer's institutional culture; and (2) keeping a local floating employee off the books prevents compliance with mandates like payroll withholdings/contributions.

Employment-law liabilities arise when local government labor enforcers bring employment claims or when a terminated floating employee sues in local labor courts (local labor courts will generally exercise some form of "long arm" jurisdiction over non-resident employers on which they can serve process). Indeed, these employment liabilities can be contagious: In Brazil, for example, an employer entity that fails to contribute to mandatory local social security and unemployment funds will expose sister affiliates to its own debts to these employee funds.

Payroll. A special employment law compliance problem in the "floating" employee context involves local laws related to *payroll*. An unregistered overseas employer with no local taxpayer identification number will find itself unable to report, contribute and withhold to the local tax authorities and to local "social funds" (state retirement, housing, unemployment, socialized medicine, workers' compensation and other mandatory welfare agencies). Outside payroll providers can *tender* these payments, but payroll providers cannot administer payroll until the client gets its required employer payor numbers. Violations of payroll requirements can come to light in an audit and are especially likely to emerge when an employment relationship terminates. Arrearages, plus interest and fines, can be surprisingly expensive.

"Leased employees." A common strategy for sidestepping all these local registration and payroll hurdles is for the overseas employer to "lease" an employee by having the would-be local floating employee get hired onto the payroll of some already up and running local employer, such as: a corporate affiliate sister entity, one of the multinational's local commercial agents or distributors, or a so-called "PEO" (professional employment organization) or other provider of HR staffing services (say, one of the international staffing firms Adecco, Manpower, Inc., Randstad, or a local-market provider).

Under a carefully structured "leased employee" (secondment or PEO) arrangement, the in-country employee gets *employed by*, and goes onto the payroll of, the local business partner while *rendering services for* the non-resident principal. The principal reimburses the nominal employer for costs (plus, usually, an administrative premium—in India, for example, staffing companies tend to charge about 15 percent). "Leased" employees can be an ideal way to resolve many of the legal issues inherent in a floating employee arrangement, but they introduce other problems, including: the extra expense, the principal's lack of direct control over the employee, the employee's reluctance to work for a third party (expect professional employees to be particularly reluctant to work for a staffing or PEO firm) and "dual employer" challenges. Also, a business operating in-country through a seconded employee remains susceptible to a charge that its operation amounts to a local "permanent establishment" subject to commercial registration and tax requirements—especially if the leased employee transacts business on the principal's behalf and has agency authority to bind the principal, and especially if the leased employment persists for longer than some initial transition period.

Independent contractors. Another strategy for sidestepping local employment law hurdles is for the multinational employer to engage a local services provider not as a floating employee but as a floating *independent contractor* (or "consultant"). The principal can get an extra layer of protection here if its independent contractor incorporates locally and if the parties enter a business-to-business services contract with the contractor's company, not with the contractor personally.

But independent contractor status is fragile, and a contractor can easily be held a *de facto* employee. Structuring an independent contractor relationship instead of hiring someone directly is a less-than-ideal solution where the arrangement seems a subterfuge. Always ask: *If an independent contractor relationship is such a great idea, then why don't we also engage this person's counterparts, back home, as independent contractors?* Often there will be a simple answer: *Because that would never fly—these people obviously work as employees, under the applicable tests.* If the set-up would fail the employee vs. independent contractor tests back home, it will also likely fail the tests in the host country: These tests are surprisingly similar from country to country. The law in many countries tends not to defer to parties' choice of labels when determining the true nature of the relationship, but rather imposes a "facts and circumstances" test. (All this having been said, though, in a minority of countries like Israel and India, the analysis may be theoretically similar, but the level of scrutiny may be much less, or there may be more viable vehicles for structuring an independent contractor relationship.)

Even a business operating in a country through a legitimate independent contractor remains susceptible to a charge that it runs a local "permanent establishment" subject to commercial registration and tax requirements, especially if the independent contractor transacts business for, or has agency authority to bind, the principal. Liability for getting this wrong, either mischaracterizing a *de facto* employee as a contractor or ignoring the "permanent establishment" ramifications, can be huge. Exposure becomes especially likely when the relationship ends. Yet in those situations where a principal *can* implement a legitimate independent contractor relationship that avoids being held a local permanent establishment, the independent contractor approach might be an excellent resolution to the floating employee conundrum. Usually this will be possible where the overseas services provider is truly an independent agent, free to work for others, paid by the task, not subject to the principal's supervision or discipline, not identified as an employee of the principal and not compensated like an employee.

Immigration Law

A multinational faces immigration law challenges when a floating employee (or independent contractor) will live outside his home country, such as when the employer sends an expatriate to the new start-up operation. Non-citizen resident employees in a new host country need a residence visa, a work permit, or both, and any foreign assignment—no matter how brief—needs to address immigration. In countries including Brazil, Saudi Arabia, UAE, Kuwait and Qatar, an inbound expatriate immigrant needs to find some local national (or locally registered business) to act as a visa/work permit sponsor. Often the sponsor must hire the expatriate and the visa/work permit is tied to the job. In these cases, our "leased employee" scenario (out-of-country principal employer arranges secondment with in-country visa sponsor) poses a problem if the local visa/work permit prohibits the sponsored employee from serving another employer. Another issue is caps on immigrants: A number of countries (Brazil is one) cap the percentage of workplace that can be foreign citizens.

Part 2: Checklist of Issues for Launching HR Operations in a New Country

Having looked at start-up issues largely from a corporate perspective, we now turn to an inventory of the human resources issues that arise as an employer begins to employ its first employees in some new country. Here is a checklist of the HR questions that can arise when a business expands into new jurisdiction. *Answers* to the questions, of course, vary according to the country at issue. This checklist is broken into five stages of starting up a new operation abroad.

Stage 1: Business Structure and Contracting

Employer corporate entity: When entering a new country, the first legal question is *Which corporate structure to use for in-country operations—a representative office, a branch, or a subsidiary?* Although this is a corporate law question, employment issues come into play. Carrying on business overseas may well subject the parent entity to local tax liability as a "permanent establishment" and expose parent-company assets to host-country claims. Set up any such local entity before doing any hiring, to avoid later having to transfer staff into some separate entity, which can raise difficult issues of transfer liability. (See discussion, Part 1.)

Subsidiary structure: Where incorporating a local subsidiary makes more sense than registering a local branch or representative office, structuring a host-country subsidiary will trigger employment issues. Different types of host-country corporations (in Germany, for example, *AG vs. GmbH*) can carry different collective labor/employment obligations. In Latin America multinationals sometimes incorporate a local "services" company—separate from the local operating subsidiary—to manage liability under local employee profit-sharing laws that require paying employees a percentage of annual employer profits. Account for these issues in setting up the local entity.

Agents/officers: Setting up a host-country corporate entity presence usually requires designating in-country shareholders, selecting in-country directors, issuing local powers of attorney and appointing local agents for process. On-the-ground, in-country employees are usually the most logical choices to fill these positions. But the problems tend to arise later. Multinational headquarters have been held hostage overseas by disgruntled ex-employees clinging onto stock interests, directorships, powers of attorney, or agency controls over a local subsidiary corporate entity because, under law in many countries, firing an employee does not automatically dissolve these separate corporate relationships. Before bestowing corporate powers on host-country employees, work out an *exit strategy,* in case of an unfriendly separation.

Independent contractors: When taking first steps in a new country, engaging "independent contractors" instead of employees may seem like an attractive strategy. However, a "freelancer" working abroad as a *de facto* employee can be deemed an employee by operation of law, regardless of the text of the contractor agreement—thereby exposing the principal to significant tax and other liabilities. And even if the contractor is held to be a self-employed agent, local laws may still impose restrictions on termination. Plan accordingly. (See discussion, Part 1.)

Vendor partners: A business entering a new country often needs to contract with local partners if only to outsource functions like payroll, accounting, or janitorial services. Factor in the employment law exposure here if outsourced employees might later claim also to work for the principal as a "dual employer" (a particular issue in Latin America). Separately, some countries (chiefly Brazil) expressly limit outsourcing of this sort.

Foreign entity monitoring: Some multinationals' overseas heads-of-office have "gone bad" and abused autonomy, paid bribes or embezzled money. These problems arise more often after headquarters has put the foreign office on "auto pilot." Cede no more autonomy to an overseas office head than to a domestic counterpart. From the beginning, put in place tough accounting, oversight, audit, Sarbanes-Oxley and Foreign Corrupt Practices Act controls.

Stage 2: Benefits/Compensation

Benchmark: To hire people into an operation in a new country requires attracting in-country employees into a business which, as yet, lacks a market presence—and an "employment brand." Under these conditions attracting host-country talent without overpaying requires careful benchmarking of local benefits and compensation. Get a breakdown by "minimum expected package," "standard expected package" and "rich expected package." And before setting initial compensation, factor in *vested rights:* Countries tend to restrict an employer's flexibility to roll back pay or benefits granted up front.

Statutory benefits costs: Engage an experienced in-country payroll provider and then ask about total payroll costs *beyond wages.* Budget for applicable "statutory benefits" and "social costs" like social security, housing funds, disability funds, profit sharing, provident funds, premium-paid vacations and thirteenth-month bonus. These can add a surprising amount to base pay.

Customary benefits: Most countries offer government payor ("socialized") medicine, so employer-provided health benefits may not be an issue—except that, increasingly, employees in certain countries expect supplementary health insurance. Separately, the social security retirement benefit in some countries replaces a high enough percentage of final average pay that in some (not all) positions, private pensions may be unnecessary. But in many countries employers are expected to give *other* customary benefits, ranging from bus transportation to meals to cars to housing. Find out which benefits are customary and how much they cost.

Stage 3: Hiring Issues

Hiring strategy: Find out which strategies and tools will work in the target country to attract and retain bilingual multinational-quality local talent. How effective are host-country recruiters?

Job application form: Adapt an organic in-country job application form for the new operation, or else modify the headquarters application form appropriately. Ensure any globally accessible Web-based job application complies in-country.

Background checks: In many countries data privacy and criminal laws tightly regulate background checks and pre-hire screening—and limit the availability of good information about applicants. Formulate a host-country background check strategy, factoring in what can be done legally and practically.

Affirmative action: Diversity has gone global. Some jurisdictions actually impose affirmative action hiring requirements that outstrip U.S. rules: South African affirmative action regulations force employers to file sensitive government reports that distinguish "African" employees from "Coloureds." German laws require hiring the disabled or paying for an exclusion. Indian laws promote hiring low-caste employees. Further, many multinationals have adopted their own in-house global diversity policies. Be sure to comply.

Expatriates: Be sure expatriates sent in have visas/work permits, and are employed on terms compliant with local laws and with the company's expatriate policies.

Stage 4: Written Employment Contracts

Contractual document: Laws in many countries require signing some employment contract or agreed-offer letter or, at least, giving employees a written "statement of terms and conditions of employment." Even where not mandated, written employment contracts outside the U.S. protect employers by disproving employees' version of what was the oral employment arrangement. In many countries a detailed employment contract also plays the role that employee handbooks play in the U.S. But do not transplant a U.S. job offer form letter with a U.S. employment-at-will clause. Use an organic in-country form contract, or else modify a U.S. form appropriately. A new in-country start-up should add in a right to assign the relationship to an entity incorporated later (in case of any corporate shuffle), plus a right to change the place of work (in case of an office move).

Probation: Employee probation periods, where available, can offer employers flexibility (at the outset of employment) from rigid restrictions against firing. But understand the limits: In Japan, for example, even a probationary employee is not employed at-will.

Fixed-term: Fixed-term employment contracts, rolled over for successive terms as necessary, can also offer flexibility. But most countries restrict serial roll over of consecutive fixed-term contracts. Check local limits. China and France recently issued fairly complex rules in this regard.

Job titles: In place of the U.S.-law distinction between "exempt" and "nonexempt" employees, employment rights outside the U.S. can tie into job *position.* Bestowing a title like "Managing Director" can affect whether certain host-country employment laws, agency powers and "sectoral" collective agreements reach an employee. Account for this in bestowing titles.

Restrictive covenants: If non-compete/confidentiality/non-solicit restrictions are important, get a locally enforceable clause. Never transplant a restrictive covenant clause from abroad, because enforceability will turn on national law. Many countries require paying extra consideration in exchange for non-compete obligations. France and Germany impose especially tight restrictions in this regard.

Employee inventions: In the absence of special contract provisions, Japan, Argentina and some other countries grant generous rights to employees who develop and register intellectual property—even while working on the clock. Ensure employment contracts quantify and contain any such exposure.

Mandatory retirement clause: In most countries—even many with age-discrimination laws—mandatory retirement remains legal and widespread, but can be tricky to implement. In October 2007 the EU Court of Justice affirmed that forced retirement does *not* violate the EU age-discrimination prohibition of EU Directive 2000/78. If mandatory retirement makes business sense for a new in-country operation and is consistent with the company's code of conduct, be sure to build any retirement mandate into individual employment contracts from the beginning.

Stage 5: HR Administration

Handbook/policies: Bringing employees on board in a new country requires having an HR structure in place, which means *policies.* A U.S.-style employee handbook is often a bad substitute for organic in-country policies. Instead, issue locally required HR mandates, such as the "work rules" of Japan and Korea. Use any locally advisable HR forms, such as the UK's overtime opt-out. Actively check to be sure the new local policies are consistent with any globally applicable code of conduct or policies that headquarters may have issued.

Translations: English is not quite the *lingua franca* it may seem to be. Laws in some jurisdictions (for example France, Belgium, Quebec) mandate that HR communications be in the local language. Penalties for violating these language laws can be severe, especially under France's *loi toubon.* Even where there are no such laws, local-language HR communications promote comprehension and enforceability in court and before government agencies and employee representatives. Translate accordingly.

Compliance: Comply with host-country labor/employment laws. Start by checking what laws affect "on-boarding" employees, such as mandates as to: hours; breaks; holidays/vacations; weekend closings; paid days off; parental leave. In Europe it is illegal to withhold benefits from part-timers. If the new start-up operation has no in-country office as yet, research applicable laws regarding *working at home.*

Employee representatives: U.S. "union avoidance" strategies are rarely exportable. Overseas, worker representatives (trade unions, works councils) can be ubiquitous and "sectoral" collective agreements often reach even non-signatory employers. In countries like Mexico, some employers actually *invite in* acceptable "white unions." Tailor a collective employee representation strategy.

Human resources data: Data protection/data privacy laws in many places restrict transmitting employee data out of country, even to an employer's own headquarters. Implement compliant practices such as under European Union "model contractual clauses" (or "safe harbor" or "binding corporate rules").

In-country insights: The best "ounce of prevention" is learning from the mistakes of those who went in before you. When gathering answers to the questions on this checklist, ask your local in-country contacts a catch-all question: *Which human resources and compliance mistakes do you most often see being made by companies coming in from abroad?*

Conclusion

Starting up business operations in some new foreign country—even where a business tiptoes in by engaging just a single service provider working from home—opens a Pandora's box of legal issues. While there is no easy way around all the problems here, there are some shortcuts and efficient strategies that let careful multinationals meet international goals efficiently and cost-effectively.

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What U.S. Corporations with Italian Subsidiaries Need to Know About Italian Employment Law

By Raffaella Betti Berutto and Filippo Pucci

1. Establishing a Presence in Italy

A first issue that a U.S. corporation wishing to conduct business in Italy has to face is whether and how to establish a presence in Italy. Three options are available: to set up a mere representative office, a branch or a subsidiary.

A representative office merely serves the purposes of advertising the company's business in Italy, but it may not be used to actually conduct business; otherwise it may run the risk of being qualified as a permanent establishment of the U.S. corporation in Italy. If this is the case the foreign company will have to comply with Italian tax law and will be subject to tax penalties. If acting through a representative office, the U.S. corporation will have to appoint an Italian company representative (usually a payroll adviser) duly empowered to conduct the relevant activities and eventually to take care of the administrative burdens related to management of personnel directly hired by the representative office (e.g., to obtain a tax identification code; to complete the registration of employees with INPS [Italian Social Security Agency] and INAIL [Mandatory Insurance Agency], etc.).

A branch is a local business office, which does not have a legal personality of its own and thus shares the same legal personality of the establishing company. It is managed by a branch manager and has very light corporate obligations (e.g., it does not require a local Shareholders or Board of Directors or Statutory Auditors Meetings, nor does it require the drafting and approving of annual financial statements, etc.).

A subsidiary is a company with its own legal personality. It can take the form of a Limited Liability Company (SRL) or of a Joint Stock Company (SPA), depending on whether the business is small and run by a limited number of quota holders or, instead, it has a large number of shareholders and intends to trade on the capital market.

The decision as to which kind of presence to establish in Italy mainly depends on the actual services that the U.S. company intends to carry out in Italy and the costs and administrative burdens that it is ready to bear in the start-up phase.

2. Staffing the Office

Once a presence has been established, a U.S. company must then choose how to best structure the local office.

Under Italian law workers are divided into two categories: employees and self-employed workers. The former are those who actually benefit the most from the protection granted by labor laws (e.g., protection against unfair dismissal and in case of illness, limited working time, mandatory enrollment with INPS and INAIL with consequent payment of the relevant social security contributions [on average 43% of the employee's gross salary, of which 30-35% to be paid by the employer and the remaining part by the employee], etc.). In case of dispute, Courts rely on a number of criteria to establish whether the nature of the relationship is subordinate or self-employed, such as: the level of control exercised by the employers over the performance of work and the actual level of integration of the workers into the organization.

As far as employees are concerned, the company has essentially two options to staff its office:

- to second employees; or
- to hire employees.

Seconding employees presents the advantage for a U.S. company to staff the local office with employees who already gained significant experience working at the parent company. This is particularly useful during the start-up process and especially when executives and high-ranked white collar employees are seconded. Secondment, however, is a temporary legal arrangement and cannot be for an indefinite period of time. In order to be seconded in Italy, a U.S. employee will have to obtain a working visa, which is usually easily granted for skilled employees and executives, provided that the employees have been working for the seconding company for at least 6 months.

Hiring local employees is usually the preferred option, especially with regard to blue collar and low-level white collar employees. In this case the employer may recruit workers by simply welcoming job applications or it may choose employees that have registered with a local labor office, which maintains a list of the unemployed.

Also, an employer is allowed to directly recruit foreign nationals, provided that the recruiting process is not discriminatory against potential applicants on the ground, for instance, of race, sex, ethnic origin, etc. EU nationals do not need a work permit to work in Italy, but just to register with the registry office of their place of residence. For non-EU nationals, the process is more complex:

- the employer has to apply to the Immigration Office (*Sportello Unico per l'Immigrazione*) for a temporary work permit, providing information on the employee to be hired and on the company/employer;

- other than for highly skilled workers and executives, the issue of a temporary work permit is conditional upon: (i) the Immigration Office being satisfied that: the hiring does not exceed the immigration threshold established every year by the Ministry and (ii) the vacancy cannot be filled by a EU national already residing in Italy and enrolled with the Labor Office;

- the working permit is, then, forwarded to the Italian consulate abroad so as to allow the employee to apply for a work visa;

- once in Italy the employee has to register with the local police office where he is residing and obtain a stay permit (*Permesso di Soggiorno*).

Also relevant in case of a secondment or hiring of a U.S. national in Italy is the USA–Italy Social Security Totalization Agreement, which, upon occurrence of certain conditions, allows an employer to avoid a double payment of social security contributions and grants the employee the opportunity to totalize social security contributions accrued in USA and Italy and resulting benefits.

3. The Employment Relation

In Italy employment relation is highly regulated. Besides international and EU sources, employment relationships are governed by certain general provisions of the Italian Constitution and those contained in statutes (particularly Law. No. 300/1970 known as "Worker's Statute"), collective agreements (both at national and company level), individual contracts of employment and custom.

A primary role in the regulation of employment relationships is played by national collective agreements, which are entered at sector level (e.g., Industry Sector, Credit Sector, etc.). The bargaining process involves, on the one hand, the trade union associations belonging to a specific sector and representing the employers and, on the other hand, the employees. Collective agreements are legally enforceable only if the employer and the employee are members of the signatories unions. Courts, however, usually accept to refer to collective agreements to determine which provisions regulate the employment relationship, even if the parties are not signatories to the agreement.

The content of a collective agreement comprises three main elements: first, it determines the provisions, usually very detailed, which regulate the individual employment relationship (e.g., minimum wage, working time, duration of probationary period, specific grounds for dismissal and notice period). Secondly, it sets the collective rights (such as the right of information and consultation of trade unions). Thirdly, it contains rules about how future collective relations should be conducted, such as how and when bargaining should occur between the parties. Collective agreements are intended to supplement statutes and the parties cannot contract out unless the provisions set in the individual contract of employment are more favourable to the employee.

The preferred legal arrangement for work in Italy is the law of contract. In case of dispute, the employer has the burden to prove the content of the individual contract of employment. Therefore, employment contracts are entered into in writing. The content of the individual contract is usually very limited (e.g., the name of the parties, the place of work, the hiring date, level of employment and duties assigned, duration of probationary period, if any; working time and notice period), because it refers to and incorporates the applicable collective agreement. More articulated rights, benefits and obligations (such as restrictive covenants; confidentiality obligations; parachute obligations, etc.) are usually negotiated and included in the executive's employment contract.

Law allows the employer to enter into different types of employment contracts (such as Apprenticeship contracts, Part time contracts, Employment contract with a term, Employment contract with "no time limit," Job on-call contracts, Job sharing, etc.) provided that certain specific requirements are met.

Changes or amendments to the contract must be mutually agreed to by the parties, with the exceptions of those minor changes that may be considered as the expression of the discretionary power of the employer to direct production conferred to the employer by article 2104 of the Italian Civil Code.

A peculiar aspect of Italian law is that a range of employment law requirements and additional protections for employees are triggered when a company employs more than 15 employees:

- the employer must hire a specified proportion of disabled workers, orphans, widows and refugees;

- employees may elect a works council to represent their interests;

- in case of unfair dismissal the employee is entitled to be reinstated in his job;

- if the employer needs to make 5 or more people redundant it must comply with a collective dismissal procedure;

- trade unions have to be informed and consulted before transferring the business.

Most provisions of Italian law are mandatory. Therefore, even if the parties were to choose a foreign law as the governing law of the employment relationship, most rules would still apply.

4. Workers' Representation in the Workplace

The Italian Constitution grants to individuals a right to form trade unions, to become member and to carry out union-related activities. It is currently possible to have two main forms of workers' representation in the workplace: the RSA and RSU.

RSA is the basic legal form of workers' representation. RSA may be established in every sector (commercial and industrial) provided that: it is established by the trade unions that signed the collective agreement applied by the employer and that the employer is staffed with more than 15 employees. There are no rules governing the election procedure or the length of the unions' representative office.

RSU may be established in the industrial sector and if the employer employs more than 15 employees. The initiative to establish a RSU is taken by the main trade unions (CGI, CISL, and UIL), trade unions that signed the collective agreement applied, or other trade unions meeting certain requirements. RSUs' members have to be elected democratically and the number of members to be appointed varies depending on the headcount of the business. A member of the RSU holds his office for 3 years and can be re-elected.

Italian law recognizes a number of rights to trade union members and representatives (e.g., right to carry out trade union activities, assembly, protection from discrimination on grounds of trade union membership and activities, time-off and special protection in case of relocation).

Law and collective agreements also provide for the rights of work councils to be informed and consulted in a number of exceptional circumstances (e.g., in the event of a transfer of undertaking or of a going concern, resort to *Cassa Integrazione Guadagni* [i.e., a social unemployment scheme]). However, EU legislation recently introduced an ongoing obligation to inform and consult with work councils over specific matters (e.g., in case of decisions of the employer likely to lead to substantial changes in work organisation or in contractual relations).

5. Termination of Employment Relation

One of the most peculiar aspects of Italian employment legislation that U.S. company should be aware of is that the employment relation can be lawfully terminated in Italy only for a "just cause" or a "justified reason."

A just cause exists in case of "serious misconduct" of the employee which affects the "trust" which should underpin the employer-employee relationship, to the extent that it is no longer possible to continue the employment relationship, not even on a temporary basis. In this case, the employee is not entitled to any notice period, but retains the right to obtain the other statutory termination indemnities (these also include the so-called TFR, which is a sort of deferred compensation regularly accrued by the employee during the employment relationship, which broadly accounts for 1 month's salary for every year of service and becomes due at the end of the employment relation regardless of the cause of termination).

A justified reason may occur in case of a "serious breach" by the employee of his/her contractual obligations (e.g., failure to comply with the employer's instructions, repeated unjustified absence from work, poor performance, etc.) or in case of reorganization needs of the business, such as an headcount reduction arising out of a reorganization of the production activities, which implies the elimination of the employee's job position. If the dismissal is grounded on a justified reason the employee is entitled (in addition to the TFR and the other termination indemnities) to the notice provided by the collective agreement or, if he consents, to payment in lieu thereof.

If an employee is dismissed without cause or justified reason by an employer staffed with more than 15 employees, he is entitled to reinstatement in his job position and the payment of damages amounting from a minimum of 5 months' salary up to the value of the salary due from the date of dismissal until the date of the reinstatement. Employees may also opt for reinstatement to be substituted with an additional compensation equal to 15 monthly salaries. If the employer employs 15 or less employees, the employee who has been unlawfully dismissed is entitled to be re-hired or, depending upon the choice of the employer, to the payment of damages ranging from 2.5 to 6 monthly salaries.

There is no qualifying period to benefit from the aforesaid protection. However, the employee is required to challenge the dismissal within 60 days from the date of receipt of the written communication of termination. Special rules apply in case the employee is pregnant.

In addition to the cases outlined above, the employment relation with an executive can be terminated with notice by the employer also for a "justifiable reasons" (such as redundancy, poor performance, etc.). Executives are never entitled to reinstatement in their job position. However, they are entitled to claim damages in a measure which varies upon the length of service and the age of the executive, according to the criteria set in the applicable collective agreement.

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The Pro Bono Partnership: Pro Bono Opportunities for In-House Attorneys

By Maurice K. Segall

Contrary to popular belief, there are many excellent opportunities for in-house counsel to engage in meaningful pro bono activities, one of which is working with the Pro Bono Partnership (www.probonopartnership.org) to help nonprofit organizations with their business legal needs.

In this challenging economy, nonprofit organizations have been stretched extraordinarily thin by tight budgets and decreasing staff, yet there's an ever-increasing demand for their services from growing segments of the public. Consequently, nonprofits must rely upon outside contributions and pro bono expertise to run efficiently.

One indispensable service that nonprofits cannot do without is sound legal assistance to address their organizational legal needs. Nonprofits have the same business legal needs as for-profit entities. However, given their extraordinarily limited resources, they typically don't have the funds to pay for necessary legal advice. They often turn to lawyers on their board who may not have the time or subject matter expertise to effectively handle the nonprofit's matters. Or, they simply proceed without any advice at all.

The Partnership, a 501(c)(3) charitable organization with offices in White Plains, NY, Stamford, CT, Hartford, CT and Parsippany, NJ, helps to address this problem. Founded by members of what was then known as Westchester County, NY—Fairfield County, CT Corporate Bar Fund (now WESFACCA, the area chapter of the American Corporate Counsel Association), the Partnership's mission is to encourage pro bono activities by the in-house bar, by offering lawyers discrete and manageable pro bono projects for the Partnership's clients, nonprofit groups serving the poor and disadvantaged and providing important social services in our communities.

Unlike "traditional" pro bono legal matters, which are generally litigation-based projects for individuals (such as divorce and other family law matters, immigration matters, landlord/tenant proceedings, and criminal and asylum matters), the Partnership is designed to engage in-house lawyers by offering non-litigation based projects that are within the attorneys' areas of expertise. With ongoing back-up and support from the Partnership's legal staff, experts in the area of tax-exempt organizations, in-house attorneys regularly provide counsel to nonprofit organizations on a broad range of legal issues such as reviewing contracts, advising on corporate governance matters, assisting with a wide range of employment issues, environmental law issues, intellectual property matters, real property matters, mergers, bankruptcies and dissolution, and nonprofit/tax-exempt issues.

Examples of projects for the Partnership's nonprofit clients include:

- Negotiating a contract for a nonprofit working with victims of domestic violence.
- Revising the bylaws for a group that builds affordable housing.
- Reviewing personnel policies for a nonprofit food pantry, and advising on an employee termination.
- Consulting with a nonprofit group home regarding whether to accept the donation of potentially contaminated land formerly used as a gas station and car dealership.
- Helping a nonprofit senior center obtain protection for its logo and slogan, and providing a legal review of the Center's website.
- Representing a small HIV/AIDS organization as it merges with a larger, multi-faceted social service agency.
- Assisting a new program offering parent education and support programs to become an independent nonprofit, tax-exempt organization.

Rick Hobish, the co-founder and Executive Director of the Partnership, states: "Our volunteers represent the best of our profession, and what the Partnership stands for—maximizing the expertise of corporate and law firm attorneys for the benefit of nonprofit organizations that are providing essential services and improving conditions for thousands of individuals and families in our communities. Their contributions are especially important in today's difficult economic climate, where nonprofits and the people they serve need support more than ever before."

In addition to the unique nature of its projects, the entirety of the Partnership's program is geared to addressing the needs of in-house and other transactional attorneys:

- Since the Partnership does not handle litigation matters, most projects are very discrete, not time-sensitive, and can be worked on when it best fits into the attorney's schedule.

- No minimum hours are required, and many of the projects take only a few hours or less to complete.
- Attorneys are not asked to become the "general counsel" for a nonprofit; rather, the expectation is to work on only one assigned project; if the nonprofit has additional legal needs, they are assigned to other attorneys.
- A Partnership staff attorney is assigned to co-counsel on every project, and will provide model documents, review drafts and offer other support as needed.
- In-house attorneys can be paired together on projects, or can be paired with law firm volunteers.
- If you become overburdened, the Partnership can reassign your matter to one of its staff attorneys or to another volunteer attorney.
- The Partnership furnishes liability insurance coverage for all volunteer attorneys.
- NY-admitted attorneys can get CLE credit for working on projects through the Partnership.
- Attorneys can also get involved by offering an educational workshop for the nonprofit community, by writing brief articles for the Partnership's website, or by simply answering brief "resource calls."

Nonprofit clients and attorney volunteers have high praise for the Partnership's program:

- "The pro bono assistance we receive from the Partnership's volunteer attorneys allows us to save money that we can put to our programs, helping more people who desperately need our services. If not for organizations like Pro Bono Partnership, we would have to cut back on programs and serve less people." Jason Shaplen, CEO, St. Luke's LifeWorks, Stamford, CT.
- "As the Executive Director of a small nonprofit in this world of increasing complications, I truly appreciate the existence of the Pro Bono Partnership and the volunteerism of their knowledgeable and caring professionals. You have helped us immensely." Edythe Schwartz, Executive Director, Putnam Family and Community Services, Carmel, NY.
- "I have nothing but praise for the Pro Bono Partnership! I have used your services as both a client and as one of your volunteers. I am honored to be part of such a great organization. What matters most to me when taking on a legal matter on a volunteer/part-time basis, is that I am able to get support and guidance quickly as my time is limited. Whenever I have reached out to you for help, your responses are prompt and on target which allows me to better serve the client while balancing the many demands on my time." Eric Semenetz, Esq., IBM, Armonk, NY.
- "When working for a law firm, pro bono work was a large part of my life. I was concerned when coming in house, that I would not have opportunities to do pro bono work. The Pro Bono Partnership has made it easy to do rewarding pro bono work. Thank you!" Melissa DeBernardis, Esq., PepsiCo, Purchase, NY.

Since 1997, the Partnership has supervised and supported the pro bono efforts of more than 2,000 volunteer lawyers from leading legal departments and law firms, who have worked on more than 5,000 separate legal matters for nearly 1,500 nonprofit clients in the tri-state area. The Partnership has received numerous national and local awards in recognition of its impact, including, among many others: the American Corporate Counsel Association Corporate Pro Bono Award for outstanding commitment to the provision of pro bono service; the American Bar Association/West Group Public Service Award for the most outstanding bar association program in the country providing direct service to the public; and induction into the Thirteen/WNET New York *and* WLIW21 Community Hall of Fame.

For more information or to see how you can get involved, contact Maurice Segall, Director of the Partnership's NY and Fairfield County Program, at msegall@probonopartner.org or (914)328-0674 ext. 323.

Maurice K. Segall is Director of the New York & Fairfield County Programs for the Pro Bono Partnership, a charity devoted to providing free business legal assistance to nonprofit organizations in the lower New York Hudson Valley, Connecticut and New Jersey. Maurice provides direct legal services to nonprofit groups, coordinates and supervises the work of staff and volunteer attorneys, and frequently lectures on legal issues for nonprofits and attorneys.

U.S. District Court for the Southern District of New York Holds That In-House Counsel's Inactive Bar Membership Vitiates Corporation's Attorney-Client Privilege Claim

By Steven R. Schoenfeld

On June 29, 2010, United States Magistrate Judge James Cott for the Southern District of New York, in *Gucci America, Inc. v. Guess?, Inc.*, No. 09 Civ 4373, 2010 WL 2720015 (S.D.N.Y. June 29, 2010), held that a company cannot assert the attorney-client privilege to protect communications with a U.S. in-house lawyer who failed to maintain an active state bar membership and therefore was not authorized to practice law. This decision is an important warning to companies that in-house counsel licensure is vital for a number of reasons, including maintaining the company's attorney-client privilege.

In *Gucci America v. Guess?, Inc.*, Gucci America, Inc. brought an action against Guess?, Inc. for trademark infringement and related claims arising out of the alleged use of certain marks, logos and designs. In discovery Gucci submitted a privilege log and asserted the attorney-client privilege as a basis for not producing numerous email communications with its in-house counsel, Jonathan Moss ("Moss"). At his deposition Moss revealed that he was an "inactive" member of the California Bar. The court ultimately found that Moss had not been an active member of the California Bar during the time that he had been employed by Gucci. After the deposition Gucci further investigated Moss' Bar status and subsequently terminated Moss.

Guess demanded that Gucci produce the Moss communications on the grounds that Moss was not an attorney to whom attorney-client privilege applied, given his inactive Bar status. Gucci disagreed, and moved for a protective order.

In the June 29 decision Judge James Cott held that the Moss communications were not protected by the attorney-client privilege, and denied Gucci's motion insofar as it was based on the attorney-client privilege. The court left open the possibility that Gucci could establish that the Moss communications were protected by the work product doctrine. The work product doctrine covers documents prepared for, or in anticipation of, litigation and would not require that Moss be an attorney.[1]

Gucci argued that Moss was an attorney for purposes of the attorney-client privilege because he had been a member of the California Bar, albeit on inactive status. The court rejected Gucci's argument. The court, instead, held that the attorney-client privilege applied to communications with an attorney authorized to practice law and that the attorney-client privilege did not attach to the Moss communications because Moss' inactive Bar membership was not the type of Bar membership that authorized him to practice law. In fact, the court underscored that an inactive member of the California Bar "who holds 'himself or herself out as practicing or entitled to practice law,' as Moss did, commits a misdemeanor offense under California law."

Although the attorney-client privilege can apply to communications with a person whom a client *reasonably and mistakenly* believes to be authorized to practice law, the court held that Gucci had a duty to conduct minimal due diligence to ensure that its in-house counsel was actively licensed. According to the court, at minimum, such due diligence includes: (1) confirming that in-house counsel was licensed in "some jurisdiction;" (2) that the license authorized in-house counsel to practice law; and (3) that in-house counsel "has not been suspended from practicing, or otherwise faced disciplinary sanctions." Gucci had performed no such diligence, and thus the court found that Gucci could not show that it *reasonably and mistakenly* believed that Moss was authorized to practice law. The court further concluded that "Gucci itself bears responsibility for allowing its counsel to represent its interests without ensuring that he was authorized to do so." Gucci is not the first case in which the United States District Court for the Southern District of New York has refused to extend attorney-client privilege protection to an unlicensed in-house counsel. *See, e.g., Fin. Tech. Int'l., Inc. v. Smith*, No. 99 CIV. 9351 GEL RLE, 2000 WL 1855131, at *7 (Dec. 19, 2000) (using similar reasoning in finding that attorney-client privilege may not be asserted by a corporation where its in-house counsel had passed the New York bar exam, but never completed the formal New York admission process).

Gucci and *Fin. Tech.* demonstrate the importance of in-house counsel maintaining an active law license in at least some jurisdiction. Ensuring that in-house counsel's license is active, and that in-house counsel is authorized to practice, includes verification or proof of:

- an active license upon hiring or intra-company transfer of a lawyer from a non-lawyer position to in-house counsel;
- payment of any annual license, registration or Bar membership fees, as well as required Client Security Fund assessments; and

- completion of all required Continuing Legal Education (CLE) courses in states with mandatory CLE, and the filing of all required reports showing compliance.

Such minimal diligence and compliance can avoid the consequences encountered in *Gucci* and *Fin. Tech.* Specifically, it will maintain the company's attorney-client privilege protection, and avoid the cost and delay of motion practice over whether an in-house lawyer was authorized to practice law. The individual in-house lawyer should make sure he or she has fulfilled all of the requirements for a valid license to practice law to avoid the personal consequences of job loss as well as the potential for disciplinary action for the unauthorized practice of law. *See, e.g.*, *In re Debacker*, 184 P.3d 506 (Okla. 2008) (DeBacker was General Counsel for Dana Corp. and was permitted to work as House Counsel in Ohio under Ohio rules that required payment of an annual registration fee and an active license elsewhere, but he failed to keep his Kansas and Oklahoma licenses current and was suspended by the Oklahoma Supreme Court for one year); *In re Hipwell*, 267 S.W.3d 682 (Ky. 2008) (General Counsel for Humana Inc. was suspended by the Kentucky Supreme Court for one year after it was discovered that he had failed to pay his annual Kentucky State Bar dues, required for active practice, since 1985).

Endnote

1. By order dated September 23, 2010, Judge Cott ordered that certain documents prepared by Moss in anticipation of litigation against Guess were protected by the work-product doctrine and did not need to be produced by Gucci.

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L. to R. Barbara Levi, Co-Chair of the International Section's Corporate Counsel Committee and Executive Committee Member of Corporate Counsel Section; Jonathan Armstrong, Executive Committee Member of the International Section, Duane Morris; Howard Hacker, Pfizer; Joseph LaRosa, Attorney-at-Law.

Ken Standard Diversity Internship Program Reception

Tuesday, August 3, 2010 • New York City

Photo from the Annual Reception to honor our Ken Standard Diversity Internship Awardees. L to R: Alice White, New York Power Authority, Yamicha Stephenson, Intern, Brooklyn Law School Student, Steve Younger, NYSBA President, Kenneth Standard, Epstein Becker, Namesake for the Program, Terryl Brown, New York Power Authority, Gabrielle Perez, Intern, Pace Law School Student, Avan Shah, Intern, Albany Law School Student, David Rothenberg, Executive Committee Member of Corporate Counsel Committee and Internship Committee Chair.

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ISSN 0736-0150 (print) 1933-8597 (online)

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