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An Analysis of Recent Developments & Trends

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Recent Court Decisions Identify Concerns in Drafting Releases

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Summary: Recent court decisions provide guidance regarding issues that employers must consider when drafting releases for current or former employees. This Insight article addresses claims that cannot be released by agreement of the parties, required "carve-outs" from releases, and the content of informational disclosures under the OWBPA. Failure to comply with legal obligations, some of which are discussed in this Insight, can invalidate the release and allow employees who signed the release to nevertheless sue their employers.

Releases of liability are valuable risk-management tools for employers. The basic concept of a release is that the employer provides a sum of money or other consideration in exchange for a waiver of claims that the employee may have against the employer. Releases frequently are used to avoid litigation related to reductions-in-force (RIF), as a required element of severance programs, or to resolve potential claims with individual employees. Releases also are used to settle asserted claims against employers in administrative proceedings or in lawsuits. Courts, Congress, and state legislatures have increasingly restricted circumstances in which releases can be effective or placed specific obligations on employers related to releases. This Insight article addresses several recent legal developments that employers must consider when preparing releases for departing or former employees.

Claims that May Not Be Released

There are a number of claims that cannot be released because of specific statutory provisions. For example, claims for unpaid overtime and violations of minimum wage obligations under the Fair Labor Standards Act require court or Department of Labor (DOL) supervision to be released. Similarly, most states prohibit the release by private agreement of workers' compensation and unemployment compensation claims. Thus, in the absence of litigation, an employer cannot simply agree with an employee to release claims for unpaid overtime,

workplace injuries or unemployment compensation.

Several federal courts recently have addressed whether employers may require employees to release claims under the Family and Medical Leave Act (FMLA) without court or DOL supervision. The DOL issued regulations in 1995 implementing the FMLA. One of the provisions in these regulations states: "[e]mployees cannot waive, nor may employers induce employees to waive, their rights under the FMLA."¹ The first federal appellate court that considered the waiver of FMLA claims held that this restriction did not apply to all claims. Specifically, the Fifth Circuit Court of Appeals held in *Faris v. Williams WPC-I, Inc.*² that the regulation prohibited the prospective waiver of the substantive rights under the FMLA (*i.e.*, the right to take FMLA leave) and not waiver of proscriptive rights (*i.e.*, claims of past violations or retaliation).³

In a recent decision by the Fourth Circuit Court of Appeals, *Taylor v. Progress Energy, Inc.*,⁴ the Fourth Circuit panel reinstated its prior opinion⁵ in which the court held that this DOL regulation barred waivers of *all* FMLA claims without court or DOL supervision. The employer filed a petition for rehearing after the first decision, and the DOL filed a brief supporting the employer's position. The court granted the motion for rehearing and the DOL argued to the court that it interpreted its own regulation to mean that an employer could require a waiver of proscriptive rights but not prospective rights, as the Fifth Circuit had decided in *Faris*. Surprisingly, the Fourth Circuit rejected the

¹ 29 C.F.R. §220825.220(d).

² 332 F.3d 316 (5th Cir. 2003).

³ See also *Dougherty v. TEVA Pharms. USA, Inc.*, 2007 WL 1165068 (E.D. Pa. Apr. 9, 2007).

⁴ 2007 WL 1893362 (4th Cir. July 3, 2007).

⁵ 415 F.3d 364.

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DOL's interpretation of its own regulation, determining that the DOL's interpretation was plainly inconsistent with its own regulation. The court relied on a number of factors in deciding not to adopt the DOL's opinion of its own regulation, including the language of the regulation and the statute, inconsistent positions taken by the DOL in other litigation, and indications of the agency's intent at the time of promulgation of the regulation in 1995 (during the Clinton administration).

Recommendation. This split in authority in the federal courts requires caution by employers. Employers should not include the FMLA (as well as the FLSA and state unemployment and workers' compensation statutes) in the list of statutes specifically released by the employee in a pre-litigation release. In addition to possibly invalidating the release because the employer includes claims that cannot be released, employers may expose themselves to additional liability by including unreleasable claims. For instance, there have been examples where a party has asserted that the employer committed fraud by offering the employee a release that included a claim the employer knew or should have known could not be released by private agreement.⁶ Moreover, we recommend that the employer include in the release a statement that the release does not include rights that cannot by law be released by private agreement. If the employee has asserted or is likely to assert FMLA claims, the employer also may consider submitting the release for DOL approval, although this could result in significant delay and/or a DOL investigation.

Carve-Outs

In addition to avoiding naming statutes that cannot be released in the list of claims covered by the release, employers should consider whether they should exclude or "carve-out" specific conduct or claims from releases. The Equal Employment Opportunity Commission (EEOC) has taken the position in recent litigation that an employer may not prohibit an employee from filing a charge of discrimination in a release. The EEOC views its right to investigate charges of discrimination as part of its statutory mandate that cannot be released by a private agreement between an employer and an employee. Furthermore, the EEOC considers release provisions prohibiting the employee from filing a charge to be unlawful retaliation for asserting protected rights.⁷ Moreover, the Older Worker Benefit Protection Act (OWBPA), which is contained within the Age Discrimination in Employment Act of 1967, prohibits employers from taking any action that restricts an individual from waiving the right to file a charge or participate in an EEOC investigation.⁸ The regulations under the OWBPA further restrict the rights of the employer to prevent actions to challenge the validity of a release of age discrimination claims.⁹ Thus, it is clear that a release should not restrict an employee or former employee from filing charges with the EEOC, as this alone may invalidate the release.

However, silence alone may not be sufficient. Many employees assume that a general release with a covenant not to sue prohibits them from filing a charge with the EEOC or another agency such as the National Labor Relations Board (NLRB). Based on such an assumption,

the NLRB rejected an arbitration agreement that did not expressly carve out the employee's right to file a charge with the NLRB.¹⁰ As a result, silence in a release probably is not sufficient to support the validity of a release addressing nonwaivable statutory discrimination claims.

Recommendation. An employer should specifically carve-out the right to file a charge with the EEOC, NLRB, and other similar state or local agencies from the claims covered by the release and/or any covenant not to sue contained in the release. Specifically carving out the right to file a charge does not mean that the employee can take the employer's money given as consideration for a release and still sue and collect damages. The EEOC has approved a statement in a release carving out the right to file a charge that further provided that the employee waived all right to recovery (which means that the only relief that can be obtained in such a case is injunctive relief sought by the EEOC).¹¹

The employer also may include a statement that the employee has no pending charges or lawsuits, although the employer may not require the dismissal of any pending charges as a condition of signing the release. Of course, this may appear to be particularly "sticky" if the release is meant to resolve pending EEOC or NLRB charges. In such situations, an employer may require an employee to *request* that the charges be withdrawn (the EEOC, for example, has an official form for precisely this purpose, and is supposed to encourage voluntary settlements), so long as the employer does not condition the release on approval of the withdrawal. Again, the release may provide that if the agency does

⁶ See, e.g., *James v. Vernon Calhoun Packing Co.*, 498 S.W.2d 160 (Tex. 1973).

⁷ See *EEOC v. Land O' Lakes, Inc.*, No. 06 c.v. 3828 (D. Minn. Sept. 25, 2006); *EEOC v. Eastman Kodak Co.*, No. 06-c.v.-6489 (W.D.N.Y. Oct. 11, 2006); Enforcement Guidance on non-waivable employee rights under EEOC enforced statutes, EEOC Notice 915.002 (Apr. 10, 1997).

⁸ 29 U.S.C. § 626(f)(4).

⁹ See 29 C.F.R. § 1625.23.

¹⁰ *U-Haul Co. of Cal.*, 347 NLRB No. 34 (2006).

¹¹ See *EEOC v. Eastman Kodak Co.*, No. 06-c.v.-6489 (W.D.N.Y. Oct. 11, 2006)

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not approve the withdrawal of the charge, the employee nonetheless waives any personal recovery.

There are also certain substantive rights under state law that may need to be carved out for the release to be effective.¹²

Informational Requirements Under the OWBPA

The OWBPA also requires an employer to provide employees age 40 and over with certain information for a release to be effective to waive age discrimination claims. The purpose of these information requirements is to provide an employee with enough information to allow the employee to make an informed choice whether or not to sign the release.¹³ Failure to include the proper information invalidates the release of age claims. Several recent court decisions have addressed certain aspects of these informational requirements that employers should consider, especially in regard to a group termination. A recent decision from a district court in Minnesota addresses many of these factors and should be mandatory reading for any employer considering a RIF or other group employment termination program.¹⁴

Eligibility Factors

The OWBPA and its implementing regulations require the employer to provide the “eligibility factors for the [employment termination] program.”¹⁵ Many employers state the eligibility factors for severance pay to comply with this obligation, but courts have increasingly held that the eligibility factors must be for the *employment termination* program and

not the *severance* program. Thus, the eligibility factors would be the factors that the employer used for selecting employees for the RIF (e.g., seniority, performance, job skills) rather than the eligibility for and amount of severance (e.g., signing the release, or years of service and salary). The employer also must specifically include the eligibility factors in the disclosure to the employee presented with the release. Failure to do so will invalidate the release.¹⁶

The district judge in the *Pagliolo* case provided additional guidance on the information regarding the eligibility factors that must be included on the disclosure to the employees presented with releases. The court stated that the employer did not have to list the reasons for each employee’s termination; instead, the employer merely had to list the selection criteria employed in the program in general. For the RIF involved in the *Pagliolo* decision, those factors were job criticality and performance.¹⁷ We would caution against necessarily declining to provide selection criteria used for subgroups within the decisional unit in question. Other courts might determine that employers would have to indicate the basis for decisions used in each specific subgroup if, for example, the decision-makers considered seniority in one department, and performance in another department, and the plant manager evaluated all the information in making a final decision about which employees to select for the RIF.

Decisional Unit

The statute and regulations also require the employer to inform employees age 40 and

over of the class, unit, or group of employees affected by the employment termination program.¹⁸ This can be a very difficult obligation. If the RIF is limited to a particular department, then the information obligation may not be a concern, but RIF’s rarely are that limited. RIF’s typically involve consideration of a number of facilities and departments within facilities. Individual department managers may make initial selection decisions, and those decisions may be reviewed by higher levels of management and human resources professionals. Moreover, different managers may use different selection criteria for making decisions on who to terminate in a RIF. For example, the accounting department could select employees for the RIF based on seniority, the engineering department based on performance, and the quality control department based on job skills. These decisions then are reviewed by higher management who consider performance evaluations, seniority and job skills for all employees. What then is the “decisional unit” and how must that be listed on the disclosure provided to employees selected for the termination program?

The district judge in the *Pagliolo* case addressed several of these issues. The judge determined that the employer’s distribution of an undifferentiated list of employees chosen for the RIF and those who were not was insufficient to comply with the OWBPA regulations. The employer considered employees based on different corporate units and on a regional basis. Yet the employer never defined the decisional unit for the employees, and the court decided that the employer could not expect the employees to identify the decisional unit based on a mere listing of thousands of

¹² See, e.g., *Edwards v. Arthur Andersen*, 142 Cal. App. 4th 603 (Aug. 30, 2006), *petition for review granted*, 52 Cal. Rptr. 3d 86 (Nov. 29, 2006) (right to reimbursement for business expenses).

¹³ 29 C.F.R. § 1625.22(f)(1)(iv).

¹⁴ *Pagliolo v. Guidant Corp.*, 483 F. Supp. 2d 847 (D. Minn. Apr. 4, 2007).

¹⁵ 29 C.F.R. § 1625.22 (f)(1)(i).

¹⁶ *Pagliolo*, 483 F. Supp. 2d at 861-62.

¹⁷ *Id.* at 861.

¹⁸ 29 C.F.R. § 1625.22(f)(3)(i).

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employees on the disclosure statement.¹⁹ The court also determined that the employer violated its obligation to provide information regarding the decisional unit because it excluded employees working in foreign subsidiaries even though the employer specifically considered those employees in making termination decisions.²⁰

Formatting Requirements

The OWBPA and associated regulations require the employer to provide employees selected for the group termination program with the job titles and ages of employees selected for the program and those who were not. The district judge in *Pagliolo* also found the employer made formatting mistakes in this disclosure. The mistakes included providing birthdates instead of ages for the employees listed on the disclosure. The court referred to the language of the statute and regulations that specifically state the employer must provide “ages,” and stated that the employer could not require the employees to calculate those ages by giving the employees birthdates.²¹ In addition, employers are required to provide the position (but not name) of employees selected for the group termination program and those who are not. The employer failed to comply with this requirement in the *Pagliolo* matter because it did not provide subcategories for the position (entry, intermediate, senior, and principal) and job grades. The court specifically noted that the employer included such information on a master spreadsheet used in the RIF and commonly in daily operations, yet failed to provide this information to the plaintiffs on the disclosure.²²

The employer also failed to give correct information with its disclosure about those

employees actually terminated in the RIF. The court found that the employer violated the OWBPA by making these mistakes and, therefore, the court invalidated the releases. In particular, the employer included almost 200 employees originally selected for the RIF as eligible for severance under the termination program even though those employees later accepted transfers within the company, were not terminated, and thus were not eligible for severance. This had the effect of skewing the percentage of employees terminated who were over 40.²³ Finally, the employer simply gave one plaintiff an incomplete employee list that was missing over 3000 employees, thus invalidating the release for that employee.²⁴

Recommendations: The *Pagliolo* decision highlights several obligations employers must consider when preparing the disclosure that must be given to employees selected for the RIF. These include:

- Specifically state the eligibility factors for the employment termination program on the disclosure.
- Identify the decisional unit applicable to the employee provided in the disclosure and consider whether to include other groups if higher levels of management and/or human resources were involved in the decision-making process. Companies also may consider whether they need to reveal the selection criteria used by the decision-makers of sub-groups if the criteria differ among sub-groups.
- Accurately provide job titles and ages for those employees selected for the group termination program and those considered but not selected. Identify those individuals selected for the program but

not eligible for benefits by some different designation. Employees may have been selected for the program but not eligible for benefits because of transfers, resignations, terminations for cause, ineligibility for severance or other factors. Noting these differences by footnotes or separate columns on the disclosure are two ways to provide this information.

Carefully planning is necessary to prepare the necessary documents so that employers may manage the risk of employment termination programs. The cases described above demonstrate the increasing complexity of the issues that employers must consider. Of course, there are other complicated issues associated with drafting effective releases. Consulting qualified legal counsel is critical if employers want to be sure that the compensation provided employees is worth the price.

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¹⁹ *Pagliolo*, 483 F. Supp. 2d at 858-59.

²⁰ *Id.* at 860.

²¹ *Id.* at 862.

²² *Id.* at 863.

²³ *Id.* at 856-57.

²⁴ *Id.* at 855, n.5.