Employment Law
BRIEFING

MARCH / APRIL 2017

Buyer beware
Employee contracts aren't always conveyable

EEOC goes head-to-head with race-neutral grooming policy

Burning question: Do physical tests discriminate against women?

Together we stand … or not
Workers contest enforceability of class action waiver

HALL RENDER
KILLIAN HEATH & LYMAN

Anchorage | Annapolis | Dallas | Denver | Detroit | Indianapolis | Louisville | Milwaukee | Philadelphia | Raleigh | Seattle | Washington, D.C.

HallRender.com

Buyer beware

Employee contracts aren't always conveyable

Every year, hundreds of U.S. companies are sold to new owners, and in many cases the seller's contracts transfer to the buyer. Recently, this became an issue when employees allegedly violated their former employer's noncompete and confidentiality agreements. As a result, the Eighth Circuit Court of Appeals had to decide whether the contracts were conveyable without the employees' consent.

COMPANY CHANGES HANDS

Symphony Diagnostic Services No. 1 Inc. v. Greenbaum addressed a situation in which former employees of Ozark Mobile Imaging had signed noncompete and confidentiality agreements that listed their employers as "Mobile Medical Services Inc., Ozark Mobile Imaging, Clearview Mobile Imaging, LLC and/or its affiliates." In signing these documents, the employees agreed that, during their employment and for two years after, they wouldn't:

1. Directly or indirectly engage in the mobile diagnostic business,
2. Become connected in any manner with, or be employed by a person, company, firm or corporation engaged in, the mobile diagnostic business, or
3. On their own behalf or behalf of other people, partnerships or corporations, solicit business from customers of their former employers and their affiliates.

When Ozark was sold as part of an asset purchase to Mobilex, the new owner offered the employees part-time employment. The employees rejected the offer and went to work for a competitor. Mobilex brought suit against them to enforce the noncompete and confidentiality agreements the employees had signed while employed by the previous owner.

The employees filed for summary judgment and the trial court granted their motion. Relying on a 2004 Missouri Court of Appeals decision, *Roeder v. Ferrell-Duncan Clinic, Inc.,* the trial court held that personal services contracts couldn't be assigned to a subsequent employer without the employees' contemporaneous consent. No one disputed that, in this case, the employees hadn't given their consent. Mobilex appealed the ruling.

> *Personal services contracts require affirmative actions by the employees but noncompete agreements require only that the employees refrain from certain actions.*

APPEALS COURT DISAGREES WITH RULING

The appeals court determined that under state law the noncompete and confidentiality agreements *were not* in fact personal services contracts. Therefore, the agreements were assignable to the company without the employees' consent.

According to the court, the *Roeder* case relied on by the trial court differed from the present situation. In *Roeder,* the plaintiff had agreed in an employment contract to provide medical services for his employer's sole benefit during the term of the agreement. It was that agreement the *Roeder* court found to be a nonassignable

personal services contract. But the agreements at issue in this case weren't personal services contracts because they were free-standing noncompete and confidentiality agreements that weren't part of a larger employment contract. Furthermore, they didn't require the employees to provide personal services of any kind to their former employer.

The employees argued that the agreements *were* personal services contracts because the agreements they'd signed stated that they were entered into in consideration for continued employment by the former employer. The court disagreed, finding that personal services contracts require affirmative actions by the employees but noncompete agreements require only that the employees refrain from certain actions. The fact that the employees signed the agreements in exchange for continued at-will employment didn't transform the agreements into personal services contracts.

The court also found that the employees' obligations were the same under the agreement — regardless of whether the former or new owner was enforcing it — because no additional burdens were placed on them. As such, the appeals court reversed the trial court's judgment and remanded for further proceedings as to whether the noncompete and confidentiality agreements were too restrictive upon the employees.

ENFORCEMENT IS STATE SPECIFIC

Note that the enforceability of noncompete agreements is state specific. Each state has different factors they may consider for enforcement — such as assignability, whether the employee was terminated or voluntarily resigned, restrictiveness of the agreement, scope of the restriction, narrowness of the agreement, and the agreement's duration. This means that the same noncompete agreement may be enforceable in one state but not another. ■

AN ASSET SALE'S ROLE IN CONVEYING NONCOMPETE AGREEMENTS

The outcome of a case similar to *Symphony Diagnostic Services No. 1 Inc. v. Greenbaum* (see main article) but in another jurisdiction resulted in a different opinion. At issue in D.C. District Court case *Hedgeye Risk Management, LLC v. Heldman* was whether an employee had breached his former employer's noncompete agreement when, after the company changed ownership, he left to work for a competitor.

The employee had signed a noncompete agreement, which was acquired when a new owner purchased the employer's assets. After the acquisition, the employee worked for the new owner for a period of time and then took a job with a competitor. The company claimed that, when it had purchased the former employer's assets, it had also purchased the employee's noncompete contract. Therefore, the contract was enforceable. The plaintiff company moved for summary judgment and the employee moved to dismiss the claim.

The plaintiff argued that its acquisition of intellectual talent, including the employee's services, was crucial to the value of its purchase. What's more, the asset purchase agreement stated that the former employer shall sell, convey, transfer and assign to the plaintiff company all of its right, title, and interest in the assets relating to the business. The agreement listed assets and representations and warranties, including the seller's employees. The defendant employee was on this list. However, his employment contract wasn't mentioned or referenced anywhere in the agreement.

Because the employment contract containing the noncompete clause wasn't conveyed in the asset purchase agreement with the former employer, the court decided that the plaintiff company wasn't entitled to enforce the noncompete clause. In addition, the noncompete agreement included an exception upon the termination of the employee by the employer. The court agreed with the employee that his employment had ended when the former employer's assets were sold to the plaintiff.

EEOC goes head-to-head with race-neutral grooming policy

Does Title VII protect employees from discrimination based on their hairstyles? In *Equal Employment Opportunity Commission v. Catastrophe Management Solutions,* the Eleventh Circuit Court of Appeals considered this question when an employer rescinded a job offer pursuant to its race-neutral grooming policy.

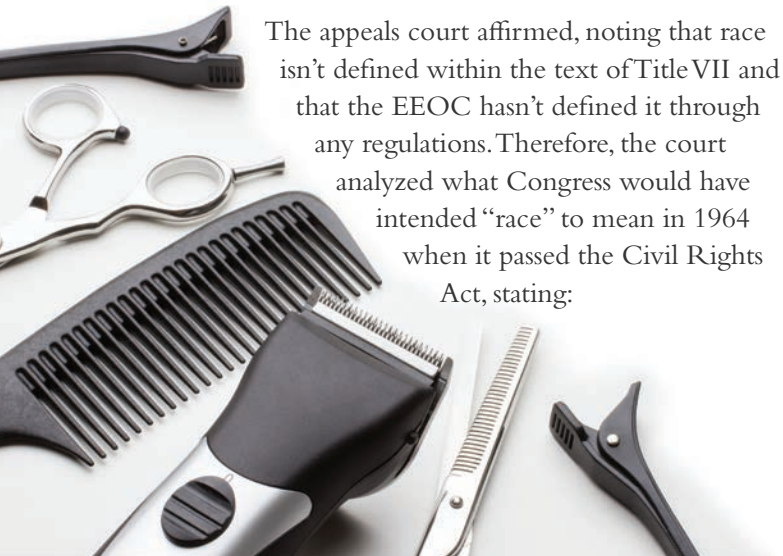
CONDITIONAL OFFER

A job applicant received a conditional offer of employment for a customer relations position that didn't involve face-to-face interaction with the public. But the applicant was told by the employer's human resources manager that she wouldn't be hired unless she got rid of her dreadlocks. The applicant refused to cut her hair, so the manager revoked the employment offer, citing the company's grooming policy.

The policy stated that employee dress and grooming was expected "to project a professional and businesslike image while adhering to the company and industry standards and/or guidelines." It elaborated that "hairstyle should reflect a business/professional image" and that "no excessive hairstyles or unusual colors are acceptable."

The Equal Employment Opportunity Commission (EEOC) brought suit against the employer on behalf of the applicant for unlawful race discrimination. The trial court dismissed the complaint and the EEOC appealed.

CONGRESSIONAL INTENTION



The appeals court affirmed, noting that race isn't defined within the text of Title VII and that the EEOC hasn't defined it through any regulations. Therefore, the court analyzed what Congress would have intended "race" to mean in 1964 when it passed the Civil Rights Act, stating:

> It appears more likely than not that "race" [in Title VII], as a matter of language and usage, referred to common physical characteristics shared by a group of people and transmitted by their ancestors over time. Although the period dictionaries did not use the word "immutable" to describe such common characteristics, it is not much of a linguistic stretch to think that such characteristics are a matter of birth, and not culture.

The court also pointed out that Title VII had been amended to protect not just religion, but "religious observance and practice," yet it hadn't been amended to expand protections for race. Therefore, the court held that Title VII protected persons with respect to their "immutable" physical characteristics but not their cultural practices and traits.

POWER TO PERSUADE

The EEOC's complaint didn't allege that dreadlocks were an immutable characteristic of black people, only that they were culturally associated with race. Its claim failed, according to the court, because its allegations didn't suggest that the employer used the grooming policy to intentionally discriminate against the applicant based on race.

In support of its argument, the EEOC relied on its compliance manual, which sets forth that Title VII extends protections to cultural characteristics such as name, manner of dress and grooming practices. However, the court stated that it would defer to the EEOC's interpretation only to the extent that "it has the power to persuade." Persuasiveness is determined by several factors, including:

- Thoroughness in its consideration,
- Validity of its reasoning, and
- Consistency.

After reviewing these factors, the court stated that it wasn't persuaded by the EEOC's compliance manual because it conflicted with a previous position. In an earlier administrative appeal, the EEOC had determined that

grooming policies that prohibited dreadlocks and similar hairstyles were outside the scope of Title VII — even when the prohibition targeted hairstyles generally associated with a particular race. In the current case, the EEOC failed to offer an explanation for its change of opinion. As such, its manual wasn't provided deference or weight.

The court noted that race isn't defined within the text of Title VII and that the EEOC hasn't defined it through regulations.

Moreover, the court found that no other court had accepted the EEOC's new position when faced with similar facts. Every court that considered the issue had rejected the argument that Title VII protected hairstyles culturally associated with race. Thus, the EEOC had not met its burden in setting forth that the defendant had intentionally discriminated against the applicant on the basis of her race. However, the court did note that, because of the complexity and role of race in society, it might be a good idea to resolve the issue of what "race" means under Title VII through the democratic process.

A REMINDER

Employers should keep in mind that, while Title VII may not be interpreted to cover cultural characteristics, many federal agencies have pushed for such expansion. In addition, state statutes may offer more protections and could be interpreted to protect cultural characteristics of race. Therefore, you must continually review your organization's grooming policies to ensure they're in compliance with the law. ■

Burning question: Do physical tests discriminate against women?

In *Ernst v. City of Chicago*, the Seventh Circuit Court of Appeals decided whether the City of Chicago discriminated against female job applicants in violation of Title VII. The applicants for paramedic jobs claimed that a physical test disparately impacted women and that the city had a discriminatory intent when it implemented the test.

JUDGMENT QUESTIONED

Some experienced female paramedics applied for paramedic positions with the City of Chicago Fire Department but weren't hired because they failed the physical test. These women brought suit against the city for gender discrimination under Title VII, alleging disparate treatment and disparate impact.

A jury heard the disparate treatment claim. The disparate impact claim was argued in a bench trial. On both claims, judgment was entered in favor of the city. The paramedics appealed.

DISPARATE TREATMENT

Title VII prohibits employment actions that are motivated by intentional discrimination against employees based on sex. Such discrimination is considered disparate treatment. To succeed on a disparate treatment claim, an employee must prove that the employer had a discriminatory motive for taking a job-related action.

In this case, the paramedics appealed the trial court's disparate treatment judgment, arguing that it had set forth an erroneous jury instruction. The instruction stated that, "[t]o determine that a Plaintiff was not hired because of her gender, you must decide that the City would have hired the Plaintiff had she been male but everything else had been the same."

The appeals court agreed with the paramedics. It held that the jury instruction should have focused on the paramedics' burden of proving that the city was motivated by antifemale bias when it created the physical test

that caused the paramedics not to be hired. The trial court's instruction focused on gender in the specific decisions not to hire the paramedics but didn't discuss whether the city had an antifemale motivation in creating the physical test. The appeals court found that this erroneous jury instruction prejudiced the paramedics, thus warranting a new trial with proper instructions.

DISPARATE IMPACT

The paramedics also appealed the disparate impact judgment that had favored the city. Title VII prohibits employment practices that have a disproportionately adverse impact on employees with protected characteristics, such as gender, even if the impact isn't intentional. One defense to a disparate impact claim is that the practice at issue is job-related and consistent with the employer's business necessity.

The city conceded that the physical test had an adverse impact on women. The burden then shifted to the city to show that the test was job-related and consistent with business necessity. It relied on a validity study to establish that the test was job-related. The creator of the test designed three exercises with input from the City's Fire Department:

1. Lifting and carrying,
2. A stair-chair push, and
3. A stretcher lift.

But the appeals court found that the study didn't satisfy the city's burden. It was established that stair-chairs weren't commonly used and that stair-chair pushes and stretcher lifts were more difficult than the tasks paramedics usually performed on the job. Furthermore, female paramedics' scores on the test were much lower than the male paramedics' scores. Due to such discrepancies, the appeals court decided that the city had failed to prove that the physical test was job-related and consistent with a business necessity. Judgment was reversed on the disparate impact claim and entered in favor of the women applicants.

NOT NECESSARILY NEUTRAL

The lesson of *Ernst v. City of Chicago* is clear. When creating pre-employment tests, employers need to consider whether they discriminate against one class of applicants — even if the tests seem neutral. To avoid Title VII claims, make sure tests are job-related and consistent with business necessity. ■

Together we stand … or not

Workers contest enforceability of class action waiver

Many employees are required to sign agreements waiving their right to bring a class action suit against their employer over wages, hours, and terms and conditions of employment. But most of them don't dispute the validity of such waivers. In *Morris v. Ernst & Young, LLP,* employees took their case to the Ninth Circuit Court of Appeals, appealing a lower court ruling and arguing that their employer had violated the National Labor Relations Act (NLRA).

SEPARATE PROCEEDINGS MANDATED

Employees brought a class and collective action against their employer claiming misclassification as exempt, in violation of the NLRA, and failure to pay overtime. As a condition of employment, the employer had required them to sign concerted action waivers stating that the employees would only pursue legal claims against the employer through arbitration and would arbitrate as

individuals in "separate legal proceedings." In other words, the employees couldn't join together and pursue concerted legal claims against the employer in court, by arbitration or in any other forum.

The employer moved to compel arbitration pursuant to the waivers. The trial court granted the employer's motion and dismissed the case.

LABOR ACT VIOLATED

When the employees appealed, they argued that the concerted action waivers they had signed were unlawful under the NLRA as determined by the National Labor Relations Board (NLRB). The employer responded that pursuant to the Federal Arbitration Act (FAA) the waivers were enforceable arbitration agreements.

But the appeals court sided with the employees. It held that the waivers the employees were required to sign violated the NLRA by interfering with the right of employees to pursue concerted work-related legal claims. The court gave "considerable deference" to the NLRB's interpretation of the NLRA that employers violated the act when they required employees to sign agreements that precluded them from filing joint, class or collective claims addressing their working conditions in any forum.

The court further stated that the NLRB was correct in finding that the agreement requirement of pursuing claims only as individuals and in "separate legal proceedings" interfered with the employees' Section 7 and Section 8 rights under the NLRA. Sec. 7 gives employees the right to collectively seek to improve working conditions. Sec. 8 prevents employers from defeating employees' rights by requiring employees to pursue their claims individually. Therefore, the "separate proceedings" section of the waiver was unenforceable, according to the court.

ARBITRATION ACT INTERPRETED

The court also disagreed with the employer's argument that the FAA required enforcement of the waivers. The FAA requires courts to enforce arbitration contracts according to their terms and on a level equal to other contracts. Although the FAA favored enforcement of arbitration agreements, the court held that the FAA couldn't be constructed to allow waivers of NLRA rights, because the statutes would then be in conflict.

The National Labor Relations Act gives employees the right to collectively seek to improve working conditions.

For the court, the waiver's arbitration requirement wasn't at issue, but the ban on concerted activities was. When the defense of illegality is raised, the FAA treats an illegal provision in an arbitration agreement just as it would an illegal provision in another type of contract. The offending provision can be deleted or a court can decide to decline enforcement of the entire contract. In this case, the court vacated the trial court's determination and remanded to determine whether the arbitration agreement's "separate proceedings" clause was severable from the rest of the contract.

NO CONSENSUS

Circuit courts have been split over the enforceability of class action waivers that demand arbitration as the venue for redress because of potential conflict between the NLRA and FAA. Therefore, employers need to ensure that their class action waivers are enforceable in their jurisdictions. Otherwise, even after signing waivers, employees will be able to file class and collective actions against their employer. Such actions can be very costly to defend when compared to single plaintiff claims and arbitration. ■

A message to our clients and friends …

The attorneys in our Employment and Labor Section are available to answer your questions about the articles in the Briefing. We also stand ready to respond to any other questions you might have. It has always been our goal to provide timely and practical advice whenever and wherever a client has a problem. You can contact each of us directly. Call us or send us an email message. We will be there for you.

"Above all, we are at your service …"

HALL RENDER
KILLIAN HEATH & LYMAN

Our Professional Client Services

- On-site management training
- Policy development & review
- Litigation and appeals
- EEOC representation
- Recruitment & hiring guidance
- Immigration
- Arbitration
- Mediation
- Union avoidance
- Employment contracts
- Wage & Hour
- Collective bargaining
- Discipline counseling
- Reduction in force counseling
- Severance agreements
- Workplace harassment
- Pensions & Benefits
- ADA, FMLA, ADEA, WARN, ERISA
- OSHA, NLRB, FCRA, USERRA, COBRA


Steve Lyman
(317) 977-1422
slyman@HallRender.com


Bruce Bagdady
(248) 457-7839
bbagdady@HallRender.com


John Ryan
(317) 977-1423
jryan@HallRender.com


Michael Kim
(317) 977-1418
mkim@HallRender.com


Jon Bumgarner
(317) 977-1474
jbumgarn@HallRender.com


Kevin Stella
(317) 977-1426
kastella@HallRender.com


Jon Rabin
(248) 457-7835
jrabin@HallRender.com


Robin Sheridan
(414) 721-0469
rsheridan@HallRender.com


Dana Stutzman
(317) 977-1425
dstutzma@HallRender.com


Larry Jensen
(248) 457-7850
ljensen@HallRender.com


Melvin Sabey
(303) 801-3535
melsabey@HallRender.com


Mark Sabey
(303) 801-3538
marksabey@HallRender.com


Sevilla Rhoads
(206) 795-6878
srhoads@HallRender.com


Jennifer Gonzalez
(248) 457-7840
jgonzalez@HallRender.com


Jarrod Malone
(317) 977-1494
jmalone@HallRender.com


Mary Kate Liffrig
(317) 977-1455
mliffrig@HallRender.com


Bradley Taormina
(248) 457-7895
btaormina@HallRender.com


Charlotte Fillenwarth
(317) 977-1476
cfillenwarth@HallRender.com


Nicholas Johnston
(317) 429-3618
njohnston@HallRender.com


Lindsay Ramsey
(317) 429-3637
lramsey@HallRender.com


Fred Bachmann
(317) 977-1408
bachmann@HallRender.com


Bill Roberts
(502) 568-9364
ebplans@HallRender.com


Calvin Chambers
(317) 977-1459
cchambers@HallRender.com


Barbra Nault
(907) 258-2588
bnault@HallRender.com


Grace Shelton
(317) 429-3620
gshelton@HallRender.com


Brian Sabey
(720) 282-2025
briansabey@HallRender.com