VEDDER PRICE

Labor Law

A newsletter designed to keep clients and other friends
informed on labor and employment law matters

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SEVENTH CIRCUIT CREATES NEW TEST FOR WHETHER

SMALL COMPANIES ARE COVERED BY FEDERAL ANTIDISCRIMINATION LAWS

In two consolidated cases that should cause lower courts to give greater deference to the corporate form of the small company when determining whether to count employees of affiliates toward the minimum required for coverage under federal employment discrimination laws, the Seventh Circuit Court of Appeals in *Papa v. Katy Industries, Inc.*, and *EEOC v. GJHSRT, Inc.*, abandoned its traditional four-factor test and adopted a three-question inquiry that it deemed to be simpler and more in line with the purposes of exempting small employers.

Former Four-Factor Test

As background, although state and local antidiscrimination laws may apply to employers with even one employee, the federal laws apply only to employers with a minimum of 15 or 20 employees, depending on which type of discrimination is asserted. Until recently, federal courts in the Seventh Circuit (which includes Illinois, Wisconsin, and Indiana) applied a four-factor test to determine whether employees of affiliates should be counted under the federal antidiscrimination laws. The factors considered were (1) interrelation of operations, (2) common management, (3) common ownership, and (4) centralized control of labor relations and personnel.

Interrelatedness of Affiliates in *Papa* and *GJHSRT*

The Seventh Circuit reconsidered this test in *Papa* and *GJHSRT*, where the employers had fewer than the statutory minimum number of employees for coverage, but were affiliated with larger corporations that had employees far exceeding the statutory minimum. The court observed in these cases that the operations of the employers and affiliates were heavily integrated. In fact, the affiliate set all salaries, provided a pension plan, and funded the defendant employer. In addition, their computer operations were integrated, the employer had the use of certain subaccounts in the affiliate's checking account, and the employer needed the affiliate's approval to write checks for amounts over $5,000.

Adoption of Three-Question Inquiry

Writing for the court, Judge Posner noted that the traditional four-factor test bore little relation to the purposes of exempting small employers from the anti-discrimination laws. In fact, the reason that small firms integrate their operations is the same reason that Congress intended them to be exempt from the anti-discrimination laws: the firms have limited resources. Judge Posner further observed that, under the traditional four-factor test, small employers that engaged in contractual integration with payroll firms, law firms, multi-employer pension plans, and group health insurance plans were not deemed "integrated" with the firms providing those services. He thus concluded that small firms similarly should not be deemed "integrated" merely because they affiliate with a larger, single company that provides all these services together.

Having abandoned the four-factor test, Judge Posner reviewed other cases to identify "three situations in which the policy behind the exemption of the tiny employer is vitiated by the presence of an affiliated corporation" so that the exemption should not apply. The first is where the employer neglects corporate formalities with the affiliate and grounds would exist for a creditor to "pierce the corporate veil." The second situation is where there is proof that a large company split itself into smaller companies for the purpose of avoiding liability under the federal anti-discrimination laws. The third situation is where the affiliate actually directs the discriminatory act. In these situations, Judge Posner concluded, the affiliate's employees will be counted when determining whether an employer meets the statutory minimum for coverage under the federal anti-discrimination laws.

The Seventh Circuit's decision in these two cases should cause lower courts to give greater respect to the corporate form of small companies when counting employees for purposes of the federal anti-discrimination laws.

If you have any questions regarding this issue, please call Barry Hartstein (312/609-7745) or any Vedder Price attorney with whom you have worked.

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SUPREME COURT RULES STATE EMPLOYERS NOT SUBJECT TO ADEA

The Constitution prohibits states from being sued by individuals in federal court. At the same time, the Constitution allows Congress to limit this right, known as sovereign immunity, so long as Congress acts within its power. If Congress appropriately abrogates, or invalidates, state sovereign immunity, individual citizens may sue a state or a state employer in federal court. The Supreme Court recently considered whether sovereign immunity protects states from being sued under the federal age discrimination law.

On January 11 the U.S. Supreme Court, in *Kimel v. Florida Board of Regents*, held that states are immune from suit by individuals under the Age Discrimination in Employment Act ("ADEA"). The Court held that the ADEA was an improper exercise of Congress' power under the Constitution. The net effect of this ruling is that, unlike private employers, states and state employers cannot be sued in federal court under the ADEA.

The Supreme Court used a two-step analysis in reaching its determination, focusing first on Congressional intent and the language of the statute, and then on whether Congress exceeded its power. The first inquiry was whether Congress made its intention to invalidate states' sovereign immunity "unmistakably clear" in the statute. The Court found that the ADEA reflects this intent by stating that it shall be enforced in accordance with a provision of the Fair Labor Standards Act which, in turn, authorizes employees to maintain actions against "any employer (including a public agency) in any federal or state court of competent jurisdiction."

Then the Court decided whether Congress had exceeded its authority. The Court's test is whether there is a "congruent and proportional" relationship between the injury to be prevented and the remedy adopted to rectify it. In other words, Congress must be addressing a wrong with the appropriate measures to override sovereign immunity.

Applying this standard, the Supreme Court held that

Congress had exceeded its authority because the ADEA was not enacted to remedy rampant age discrimination by public employers. The legislative history did not show real concern about age discrimination in the public sector. Further, older persons, unlike those who suffer discrimination because of race or gender, have not been subject to a history of purposeful unequal treatment, and old age is not a categorical minority because everyone ultimately will face it. The Court stated that the extension of the ADEA to the states was "an unwarranted response to a perhaps inconsequential problem." Therefore, Congress did not have the power to overcome the states' constitutional right to sovereign immunity.

Under this decision, state employers are no longer subject to suit under the ADEA. Not surprisingly, the American Federation of State, County and Municipal Employees (AFSCME) issued a statement denouncing the Supreme Court's decision, declaring that "public employees are not second-class citizens." *New York Times*, January 12, 2000. However, most states have state age discrimination statutes that cover state employment.

The rule may be no different for other public employers. The ADEA defines "public agency" as "the Government of a State or political subdivision thereof," and "any agency of…a State, or a political subdivision of a State." Thus cities, counties, municipalities, and other governmental subdivisions could ultimately be found to enjoy the same immunity as the states. Although *Kimel* does not specifically address this question, and no case has yet answered this specific question, other Supreme Court decisions infer this result.

A similar issue presented in *Kimel*, as it relates to the Americans With Disabilities Act, was accepted for review by the Supreme Court but settled, prior to decision. The circuit courts of appeal accordingly remain divided on the issue of whether states can be sued under the ADA.

If you have any questions about *Kimel* or a public employer's immunity from suit under the ADEA or ADA, please contact James Spizzo at (312/609-7705), or any other Vedder Price attorney with whom you have worked.

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RECENT ADA CASES HIGHLIGHT NEED TO BEWARE OF PERCEIVED DISABILITIES

It is widely known that federal law prohibits employers from discriminating against their employees because of known disabilities. Recent decisions have reminded employers that there also are risks when individuals are singled out due to "perceived" disabilities.

One recent case illustrative of this trend is *Heyman v. Queens Village Committee for Mental Health for Jamaica Community Adolescent Program, Inc.*, in which the United States Court of Appeals for the Second Circuit (which includes New York, Connecticut and Vermont) held that a medical clinic administrator diagnosed with lymphoma who was fired before becoming symptomatic can proceed with his ADA claim that he was discriminated against because his employer "perceived" him as disabled. The Second Circuit held that even though Heyman was not currently impaired, he presented sufficient evidence to allow a reasonable jury to conclude that he was terminated because his employer perceived him as having a physical impairment that significantly restricted him from working. The Court considered the timing of the termination, the fact that Heyman had no negative performance evaluations prior to his diagnosis, and the fact that Heyman's supervisor had died from the same ailment seven months earlier.

Soon after Heyman informed his supervisor of his diagnosis, he advised his employer that he would be late for work due to a medical appointment. Five days later, he received a memorandum asking for a meeting to discuss his role, performance, and the "level of time and commitment required to resolve the ongoing internal problems" in his work unit. He was terminated the next day at that meeting.

The United States District Court for the Eastern District of New York granted summary judgment for the employer on the grounds that Heyman failed to establish that he had a disability under the ADA because he had no current symptoms.

In reviewing the district court's dismissal of the case, the Appeals Court pointed out that the ADA defines a disability as "a physical or mental impairment that substantially limits one or more of the major life activities of [an] individual; a record of such an impairment; or being regarded as having such an impairment." The Court agreed with the lower court's analysis that Heyman was not actually disabled at the time he was terminated, but stated that the lower court paid only "scant attention" to his alternative argument that he was entitled to ADA protection because he was "regarded as" disabled.

The Court, in light of Heyman's past good performance, and the short time between his lateness because of a medical appointment and the date of his termination, concluded that a reasonable jury could find that the employer's expressed concern over the "time and commitment" needed for the job was "engendered by a fear that Heyman's lymphoma would render him unable to complete his assigned tasks, as it had [his former supervisor]."

In other recent cases, the courts have similarly refused to dismiss cases when the plaintiff produced some evidence that the employer reacted to a potential disability with fear. In a recent federal court decision in Missouri, the court refused to dismiss a case where the plaintiff's co-workers and supervisors expressed fear of contracting Hepatitis C, despite a report from the company doctor that the employee posed no health risk to others. The plaintiff's allegations that his employer believed he posed a health threat simply by his presence was adequate, the Court found, to show that the employer regarded him as substantially limited in the major life activity of working, affording him protections under the ADA.

If you have any questions about perceived disabilities or the ADA in general, please call Alan Koral in New York (212/407-7799), Barry Hartstein in Chicago (312/609-7745) or any Vedder Price attorney with whom you have worked.

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NLRB REVERSES ITSELF AND

EXTENDS ACT'S COVERAGE TO HOSPITAL'S INTERNS AND RESIDENTS

Overruling more than 20 years of precedent, the National Labor Relations Board has decided that interns, residents, and fellows (house staff) at an acute-care teaching hospital are employees and can be unionized. *Boston Medical Center Corporation*, 330 NLRB No. 30 (1999).

A union calling itself the House Officers' Association/Committee of Interns and Residents petitioned for certification as bargaining representative of the house staff at Boston Medical Center. The Regional Director dismissed the petition based on the Board's earlier decisions in *Cedars-Sinai Medical Center* (1976) and *St. Clare's Hospital & Health Center* (1977) that house staff are primarily students and therefore not employees under the Act. The union appealed to the Board with support from high-profile *amicus curiae*, including the American Medical Association, the Massachusetts Medical Society, the American Medical Women's Association, the American Public Health Association, the American Nurses Association, and the American Medical Students Association. A majority of the Board (Chairman Truesdale and Members Fox and Liebman) decided to overrule *Cedars-Sinai* and *St. Clare's Hospital* and a host of decisions following those cases. In the majority's view, while the hospital's interns, residents and fellows may be students learning their chosen medical craft, they also are employees under the Act and have the right to union representation.

In its *Cedars-Sinai* and *St. Clare's Hospital* decisions, the Board had concluded that the relationship house staff members have with a hospital is primarily to fulfill the educational requirements of state or specialty boards rather than to earn a living. Although they provide medical care to patients, they serve primarily as students and not as employees. Because their connection with the hospital is predominantly academic rather than economic in nature, their interests are not readily adapted to the collective bargaining process.

The current Board majority now finds this analysis flawed, and can uncover no basis for excluding house staff members from the Act's broad definition of employee.

They are paid a stipend for their services, the majority notes, from which federal and state income taxes are withheld, and receive paid vacations, sick leave and other benefits. The majority also gleans from the legislative history of the 1974 Healthcare Amendments (which extended the Board's jurisdiction to nonprofit healthcare facilities) that Congress assumed house staff officers would be covered by that legislation, and considers it persuasive that many state courts have found house staff to be employees under public sector labor laws.

Responding to the hospital's concerns about having to bargain over subjects closely tied to the educational aspects of its residency programs, the majority opines that the parties can confront issues of academic freedom as they would other issues in collective bargaining; if they can't resolve their differences through bargaining, "they are free to seek resolution of the issues by resort to our processes, and we will address them at the appropriate time."

The hospital argued that complex issues of joint employer status will arise because its house staff are assigned to rotations at other institutions with which it has an affiliation agreement. Noting that house staff remain part of the hospital's residency program while on such rotations and spend most of their time during their residency at the hospital's facilities, the majority deems the joint employer issue resolvable through collective bargaining and, in any event, speculative.

The hospital also argued that because nearly all of its residents and fellows leave the hospital once they complete their residencies, they are at best temporary employees, a category the Board considers ineligible to vote in representation elections because they lack a sufficient community of interest. The majority dismisses the argument, observing that the Board has never applied the term "temporary" to employees whose employment, albeit of finite duration, might last from three to seven or more years.

Finally, the majority rejects the hospital's argument that house staff members do not fit into any of the eight bargaining units defined as appropriate for acute health care facilities. Finding that house staff members possess skills common to other physicians and are qualified to perform and do perform medical procedures, the majority holds that they should be included in a bargaining unit of "all physicians."

In a short dissenting opinion, Member Hurtgen decries the majority's u-turn, which he attributes to a change in Board-member composition. He foresees a prolonged period of instability before the Board and courts resolve inevitable disputes over whether union proposals bearing on academic decision-making are mandatory subjects of bargaining. In a lengthy dissent, Member Brame quarrels with the majority's finding that residents are employees, pointing out that they work "at" but not "for" the hospital, and that their stipend is not compensation for medical services provided but financial support during a lengthy graduate education program. Brame also sees a poor fit between collective bargaining and the educational process, and warns that the majority's ill-advised decision "forces medical education into the uncharted waters of organizing campaigns, collective bargaining, and strikes."

If *Boston Medical Center* holds up as good law, its effects remain to be seen. An estimated 90,000 interns, residents, and fellows nationwide are now entitled to the protection of the Act.

For more information about this decision, contact Jim Petrie (312/609-7660) or any other Vedder Price attorney with whom you have worked.

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FEDERAL COURTS CONTINUE TO DEFINE FAMILY AND MEDICAL LEAVE RIGHTS

Simply stated, the Family Medical Leave Act ("FMLA") provides eligible employees with up to 12 weeks per year of job-protected leave for certain family and medical reasons. However, both courts and employers continue to wrestle with the issues of who is "eligible," to what extent an employee's job is protected and which family or medical reasons trigger the FMLA's protections. In recent months, several federal appellate courts have provided additional clarification on these issues.

Eligibility Determined as of Date Leave Began

To be deemed an eligible employee under the FMLA, an employee must have been "employed for at least 12 months" by the employer from whom leave is requested and performed at least 1,250 hours of service "during the previous 12-month period." In *Butler v. Owens-Brockway Plastic Products, Inc.* (6th Cir.), an employee was terminated under a "points" attendance policy. The employee alleged that her termination violated the FMLA because an earlier FMLA leave was included in the points counted against her. The district court held that the employee was not covered by the FMLA because, due to the earlier FMLA leave, she had not worked 1,250 hours in the 12 months preceding her termination. The Sixth Circuit reversed the district court's ruling, reasoning that if the eligibility determination were made at the time of the adverse employment action, employers could evade the statute by terminating employees immediately after they returned from 12 weeks of FMLA leave because those employees would no longer be eligible for FMLA leave. Therefore, the Sixth Circuit concluded, the eligibility determination must be made as of the date the leave at issue began and *not* as of the date of the adverse employment action. The First Circuit reached the same conclusion in *Duckworth v. Pratt & Whitney*.

Limitations on the Right to Reinstatement

The FMLA requires that returning employees be restored to their previous position or an equivalent position. However, the FMLA does not prohibit all terminations of employees on FMLA leave. Moreover, unlike the Americans With Disabilities Act ("ADA"), the FMLA regulations do *not* require employers to offer another available position to an employee who remains unable to perform the essential functions of his job when his FMLA leave is exhausted.

In *O'Connor v. PCA Family Health Plan, Inc.* (11th Cir.), employer PCA Family Health Plan ("PCA") terminated O'Connor during a reduction in force while O'Connor was on FMLA leave. O'Connor argued that PCA violated her FMLA right to reinstatement. The Eleventh Circuit rejected her argument, noting that the FMLA right to reinstatement is not absolute. When an employer denies an employee reinstatement at the end of an FMLA leave, the employer has an opportunity to demonstrate it would have discharged the employee even if she had not been on FMLA leave. The employer bears the burden of proving it would have taken the same action in the absence of the FMLA leave. Furthermore, the Eleventh Circuit held that PCA's earlier adoption of a policy of not laying off employees on FMLA leave did not expand an employee's legally enforceable employment protection beyond that afforded by the FMLA.

In *Reynolds v. Phillips & Temro Indus.*, the Eighth Circuit Court of Appeals affirmed summary judgment for an employer who terminated an employee on FMLA leave, then refused to reinstate him at the end of the 12-week leave period. Reynolds was terminated under the employer's three day no-call, no-show policy. Without addressing whether the termination itself violated the FMLA, the Eighth Circuit held that Reynolds had no FMLA right to be restored to his position because he was unable to perform his job at the end of the 12-week leave. The Court confirmed that the FMLA did not give Reynolds the right to be restored in a light duty position. However, employers should be cautious in applying this ruling, because the Americans With Disabilities Act may require light duty assignments as reasonable accommodations in some circumstances.

If you have any questions about these issues or the FMLA in general, please contact Vedder Price (312/609-7500).

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ONGOING *MICROSOFT* RULINGS REMIND EMPLOYERS OF RULES FOR INDEPENDENT CONTRACTORS

Many employers hire temporary agency employees or independent contractors instead of permanent employees, hoping to avoid the costs of employment taxes, benefits, and potential claims under workers' compensation, wage-hour, and discrimination laws. However, as illustrated by ongoing rulings against Microsoft, workers treated as independent contractors and even temporary agency employees can be reclassified as an organization's employees if management exercises too much control, exposing the organization to unexpected liability for taxes, benefits and damages under the employment statutes.

The U.S. Supreme Court recently denied review of the latest ruling against Microsoft, again bringing to the forefront the hazards of misclassifying workers. As background, Microsoft had a group of "supplemental" workers whom it treated as independent contractors. The supplemental workers wore badges of a different color from those of the permanent employees, had different e-mail addresses, were not allowed to assign their work to others, were not invited to official company functions, and were not paid through the payroll department but by submitting invoices. However, they worked side by side with permanent employees, performing the same work under the same supervision, using Microsoft equipment and supplies.

Earlier *Microsoft* Rulings

In 1989 and 1990 the IRS audited Microsoft and concluded that these "supplemental" workers were actually common law employees, not true independent contractors, and that employment taxes should have been paid on their behalf. Under common law, the courts determine whether workers are employees or independent contractors by evaluating various factors such as: (1) the degree of the employer's control over the means, methods, or hours of the work; (2) the source of the worker's instrumentalities and tools; (3) the duration of the relationship between the parties; (4) whether additional projects can be assigned to the worker; (5) the method of payment; (6) the extent of the training provided to the worker by the employer; and (7) whether the worker is doing the same work as the permanent employees.

In response to the IRS' reclassification, Microsoft made some of the workers permanent employees, then transferred the rest to a temporary agency and contracted with the agency for their services, discharging those who did not want to be employed by the agency. However, there was little change in the terms and conditions of employment for these temporary agency employees.

In 1993, the temporary agency employees and some of the workers who were discharged sued Microsoft for the right to participate in company savings and profit sharing plans,

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as their "permanent" counterparts did. *Vizcaino v. Microsoft Co.* Although the lower court ruled for the company, the U.S. Court of Appeals for the Ninth Circuit held that, even though the supplemental workers had signed agreements disclaiming entitlement to benefits, any of the workers who were common law employees were eligible to participate in these plans because the plans, by their own language, defined eligible participants according to whether they were "employees" under common law. The Ninth Circuit then directed the trial court to determine which workers were common law employees.

The Latest Ruling: Temporary Agency Employees

Then in 1999, the Ninth Circuit again overruled the trial court by holding that all the temporary agency employees, even those who were hired after the reclassification and had never been "supplemental" workers, were deemed to be Microsoft's common law employees and entitled to benefits. Even though they were employees of the agency, the court found, their interactions with Microsoft were essentially the same as the "supplemental" workers' had been. The court concluded that "the determination of whether the temps were Microsoft's common law employees turns not on whether they were also employees of an agency but rather on…their relationship with Microsoft." Thus, it did not matter whether the worker could also be considered an employee of the temporary agency. Therefore, all of the supplemental workers, independent contractors, and temporary agency employees were eligible to participate in the benefit plans. Earlier this year, as noted above, the U.S. Supreme Court refused to hear Microsoft's appeal.

The Need to Classify Workers Correctly

Microsoft's experience highlights the importance of correctly classifying workers to avoid unexpected liability. With regard to employee benefits, employers have been able to avoid outcomes similar to Microsoft's by making it clear in plan documents and in summary plan descriptions which workers are entitled to participate in employee benefit plans. For example, in *Wolf v. Coca-Cola Co.*, the U.S. Court of Appeals for the Eleventh Circuit held that a temporary agency employee was not entitled to participate in an ERISA plan because the plan's eligibility rules specifically excluded "individuals who perform services for the Company under an agreement with a leasing organization." Similarly, in *Capital Cities/ABC, Inc. v. Ratcliff*, the United States District Court for the District of Kansas held that a temporary agency employee was not entitled to participate because the plan specifically excluded temporary workers.

However, under the statutes governing discrimination, wages and hours, safety, and employment taxes, employers cannot create their own exclusions. Liability arises out of the employee-employer relationship as determined by the interactions between the parties, not the label of "employee" or "independent contractor." Thus, it is important that workers are properly classified according to their true status.

Consequently, workers should be hired as independent contractors only if that is how they actually will be used. For example, they should be hired to accomplish discrete projects. While the projects can be defined broadly, they should not be open-ended. Further, while the organization can establish guidelines for completing the project and specify the results, it should not control the means, methods, tools used or hours worked as it does with its regular employees.

As the *Microsoft* case demonstrates, temporary agency employees must also be treated differently than regular employees if an organization wants to insulate itself from responsibility as the employer. Direct control over these workers should be wielded by the temporary agency. For example, the employer should submit written requests to the agency describing the assignment so it can be communicated by the agency to the worker. Similarly, day-to-day supervision and direction should be exercised by the agency, including decisions regarding work assignment and discharge. Further, details of the terms or conditions of employment such as scheduling, attendance tracking, payroll, and performance evaluation should be handled by the temporary agency. The employer's involvement in any of these areas can result in a finding that a joint employment relationship exists.

If you have any questions about the independent contractor relationship, please call Bruce R. Alper in Chicago (312/609-7890) or any other Vedder Price attorney with whom you have worked.

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EMPLOYEE BENEFITS UPDATE

Articles addressing the following topics appear in the current issue of Vedder Price's *Employee Benefits Bulletin.* The *Bulletin*, with the full text of each article, is available on our web site at www.vedderprice.com.

New IRS Guidance on 401(k) Safe Harbor Rules Provides Flexibility for Plan Sponsors

The Internal Revenue Service recently issued additional guidance on safe harbor requirements for 401(k) plans. Safe harbor rules allow a plan sponsor to avoid conducting actual deferral percentage (ADP) testing for pre-tax contributions. Other safe harbor contribution rules enable a plan sponsor to avoid performing actual contribution percentage (ACP) testing for matching contributions, although the ACP test still has to be performed for any after-tax employee contributions.

The changes to safe harbor plan rules recently announced by the IRS provide increased flexibility for plan sponsors. Although some sponsors still may conclude that safe harbor formulas remain too expensive, other plan sponsors previously deterred by the lack of flexibility the IRS provided in 1998 may be encouraged to reconsider their position on the suitability of safe harbor plan design for their organization.

Stock Options and Overtime Calculations

The number of U.S. workers receiving stock options has increased dramatically as companies seek to compete for talent in a tight labor market. The increasing popularity of broad-based stock option programs, however, may be hindered by a recently released Department of Labor opinion letter. In that letter, the Department of Labor stated that gains realized from the exercise of stock options must be included in overtime calculations for employees not exempt from the overtime requirements of the Fair Labor Standards Act.

Cash Balance Plans

The popularity of cash balance plans has increased significantly in recent years. Despite the controversy generated by some conversions, most conversions to cash balance plans from traditional final average pay pension plans have been implemented without litigation or public controversy.

New Special Tax Notice for Rollovers

The Internal Revenue Code requires plan administrators to provide a notice to qualified retirement plan participants who are about to receive an eligible rollover distribution, describing the possible federal income tax treatment of the distribution. The IRS recently issued an updated model notice that plan administrators may use to satisfy their special tax notice obligations.

New Form 5500

A new and improved Form 5500 Annual Return/Report for Employee Benefit Plans makes its debut with the 1999 reporting year. This year also marks the start of the government's new computerized filing system, known as the ERISA Filing Acceptance System, or EFAS. Except for those filing electronically, use of computer scannable forms is mandatory for 1999 plan year reports, which generally are due in July 2000 for calendar year plans.

IRS Final Regulations on Electronic Communications

The Internal Revenue Service recently issued final regulations governing the use of electronic media in three areas of interest to plan sponsors and administrators: eligible rollover distribution tax notices, participant consents to distributions in excess of $5,000, and tax withholding notices. The IRS' new final regulations, combined with earlier IRS and Department of Labor guidance, are expected to facilitate the current trend toward electronic retirement plan administration.

"Look Through" Trusts as Plan Beneficiaries

With the increasing amount of wealth accumulated in qualified retirement plans, many plan sponsors are focusing on measures allowing participants to take full advantage of estate planning opportunities. One such opportunity is naming a trust as a designated beneficiary under a qualified plan.

If the trust is a "look through" trust, the joint lives of the participant and a beneficiary of the trust may be used in determining minimum required distributions. If the trust does not satisfy the look through requirements, a participant is treated as not having a designated beneficiary and minimum distributions will be made over the participant's life expectancy if the participant dies after his or her required beginning date, or over a five-year period if the participant dies before his or her required beginning date. In other words, the plan benefit may be distributed over a much shorter period of time, a result which the Internal Revenue Service may welcome but which plan participants and their beneficiaries may wish to avoid.

If you have any questions about these or other employee benefits topics, please call Tom Hancuch (312/609-7824) or Paul Russell (312/609-7740) in Chicago, or Neal Korval (212/407-7780) in New York.

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ODDS & ENDS

Title VII Trumps Commandment VI

A Catholic elementary school in Toledo, Ohio terminated a female teacher who was visibly pregnant shortly after her wedding. The parochial school invoked a provision in the teacher's contract that required her to reflect church values in word and example. A federal trial court threw out the teacher's lawsuit, but the Sixth Circuit Court of Appeals recently reversed. The appellate court said a religious organization may prohibit premarital sex, but not just for female employees, and the teacher should be allowed to try to show disparate treatment on the basis of sex. (We assume this could be shown by proving that male teachers at the school brought their visibly pregnant brides to second grade "show and tell" sessions, but were not fired.)

To Love, Honor and...What Was That Last One?

An Illinois brokerage firm hired a dealer and several of the dealer's personnel. The brokerage firm and the dealer signed a contract that said the dealer's personnel would not be retained if the dealer himself left the firm. Nevertheless, when the dealer was terminated, two of his former associates were kept on the payroll. The dealer sued for damages, arguing that the contract had required the brokerage firm to fire his former associates.

Writing for the Seventh Circuit Court of Appeals, Judge Posner ruled against the dealer, primarily on the grounds that the two associates involved had never consented to, or even been informed of, the "fire one, fire all" provision. Judge Posner compared the provision to the "discredited Hindu practice of suttee, whereby the widow is required to immolate herself on her husband's funeral bier." Moreover, Judge Posner said, in this case the associates never even knew they were "married" to the dealer.

Consumer Choice? Ay, There's the Rub!

In hiring massage therapists for its Camelback Inn Spa in Arizona, Marriott relied on surveys and past practice showing that a large majority of its customers (male and female) preferred female massage therapists. A non-hired male therapist won summary judgment from a federal district court judge, who ruled that customer preference cannot establish a bona fide occupational qualification. The judge recommended that Marriott, in future discussions with its customers, should reduce its "focus" on gender and increase its "focus" on qualifications, so that clients of both sexes might be more willing to engage the services of a male.

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