I Thought We Settled That Case?!?
Settlement Agreements and Potential Challenges to Fully Resolving Employment Disputes

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Overview

- Basics of a settlement “deal.”
- Where the impediments to a deal often lie:
  - Monetary consideration (how much);
  - Scope of release (who is released and to what extent);
  - Confidentiality/Non-Disparagement (scope, mutual or unilateral; consequences for breach);
  - Taxes; and
  - Additional terms (mechanisms for dispute resolution, venue, etc.).

Challenges Specific to Employment-Related Disputes

1. The EEOC Effect – accounting for rights the EEOC and other federal agencies want to survive post-settlement.

2. Releasing federal age claims – OWBPA challenges.

3. Properly addressing wage/hour matters in settlement agreements.

Challenges specific to employment-related disputes – cont'd

4. Taxation and related issues.

5. Non-hire/rehire provisions considerations for multi-state employers.

1. The EEOC Effect

- The EEOC's restrictions on releases.
  - Releases may not prohibit an individual from filing a charge of discrimination.
  - Other federal agencies have similar mandates.
- Restrictions on one's ability to voluntarily participate in investigations.

The CVS Case

- Dispute over whether CVS's "form" separation agreements were unlawful.
- Employee, fired from CVS, files a charge of discrimination. EEOC contends that CVS's use of its separation agreements amounts to a pattern and practice of "resisting" Title VII rights.
- Case is dismissed because the EEOC failed to attempt conciliation before suit.
- Appeal is pending at the Seventh Circuit.
- *EEOC v. CVS Pharmacy, Inc.*, No. 1:14-cv-00863, (N.D. Ill, October 7, 2014)(mem. op.), appeal to 7th Cir., No. 14-3653 (7th Cir. filed Apr. 30, 2015).

Note: CVS's Separation Agreement Contained the Following "Standard" Provision:

"Nothing in this paragraph is intended to or shall interfere with Employee's right to participate in a proceeding with any appropriate federal, state or local government agency enforcing discrimination laws, nor shall this Agreement prohibit Employee from cooperating with any such agency in its investigation."

EEOC v. CVS – The EEOC's Objections:

- **Cooperation** clause requiring employee to call General Counsel regarding any contacts from administrative agencies or related to their investigations.
- **Non-disparagement** clause prohibiting employee from disparaging the company, directors, officers, or employees.
- **Non-disclosure** clause – need approval from HR before disclosing any company-internal information.

EEOC v. CVS – The EEOC's Objections (cont'd):

- **General release** of claims including release of "charges" and claims of "discrimination of any kind."
- **Liquidated damages** clause disgorging whatever severance the employee received if she breached any of the foregoing covenants.
- **Attorney fee** clause that employee must pay CVS's attorney fees if it sued her for breach of any of the foregoing covenants.

EEOC v. CVS – EEOC's Position

- Settlement agreements must not chill protected activity.
- Broad confidentiality provisions and non-disparagement clauses must be scrutinized closely.
- Apply the objective standard: "reactions of a reasonable employee." *See Burlington Northern & Santa Fe Ry. Co. v. White*, 548 U.S. 53, 68 (2006).

EEOC v. CVS – EEOC's Position

- Lead case on the issue: *EEOC v. Cosmair, Inc.*, 821 F.2d 1085, 1090 (5th Cir. 1987):
  - "[A]n employer and employee cannot agree to deny the EEOC the information it needs to advance [the] public interest."
  - "A waiver of the right to file a charge is void as against public policy."

EEOC v. CVS – Takeaways

- CVS's separation agreement included a generic savings clause regarding non-waivable rights…
- But the combined effect of the other clauses – non-disparagement, confidentiality – plus the threat of liquidated damages and attorney fees for breach of those clauses – may result in a chilling effect on protected activity.
- Even unenforceable clauses can be perceived by reasonable non-lawyers as perfectly valid – and potentially chilling to protected activity.

The EEOC May Not Be Alone

- NLRB: "It is incumbent upon employers to use language that is not reasonably subject to an interpretation that would unlawfully affect the exercise of Section 7 rights."
  - *Brandeis Mach. & Supply Co. v. NLRB*, 412 F.3d 822, 831 (7th Cir. 2005)(internal citation and quotation marks omitted).
- SEC: Requiring employee to first notify company before communicating with agency considered unlawful.
  - *In the Matter of KBR, Inc.*, No. 3-16466, Order Instituting Cease-and-Desist Proceedings, (SEC Apr. 1, 2015).

- Financial Industry Regulatory Authority, Inc. (FINRA) – self-regulatory agency that regulates brokerage firms/exchange markets.
  - Reg. Notice 14-40: a model confidentiality provision will not restrict a party from initiating communications with a regulatory organization.

What Does This Mean for Settlement Agreements?

- Act at your own peril.
- Need to be cognizant of the positions of these agencies.
- Not clear what is truly mandatory.
- Agencies want to provide employees with as many rights as they can (even where an individual is represented by counsel and fully appreciates the consequences of a general release agreement).

Language to Consider:

- *Nothing in this Agreement prohibits Claimant from communicating with, filing a charge with, or cooperating in the investigations of any governmental agency on matters within their jurisdiction.*
- *Other carve-outs: Nothing in this Agreement affects Claimant's entitlement, if any, to worker's compensation, unemployment compensation, health insurance benefits under the Consolidated Budget Reconciliation Act (COBRA), or vested benefits under a retirement plan governed by the Employee Retirement Income Security Act (ERISA).*
- *Severability.*
- *Consider securing representations to address subsequent matters involving individual.*

- The tough question for employers: should you really do more than this?
- Example: clarify that any such aforementioned action is not a breach of the confidentiality, non-disparagement, or cooperation provisions of the release agreement?

2. Releasing Federal Age Discrimination Claims

- Federal age discrimination claims are treated differently than most other claims.
- Intention is to guard against unscrupulous employers taking advantage of older workers.
- Older workers = 40 years and up!
- A release must be "knowing and voluntary"
- Defined specifically by the federal statute – the Older Workers Benefit Protection Act ("OWBPA"). 29 U.S.C. §626(f).

Releasing Federal Age Discrimination Claims – the OWBPA

- Settlement must contain specific language to effectively release an age claim. 29 U.S.C. §626(f)(1-4).
- Clear language.
- Expressly name *Age Discrimination in Employment Act* claims being released.
- States it does not release claims that may arise later.
- Consideration *above and beyond* what worker is otherwise entitled.
- Written *direction* to consult attorney *prior* to signing.
- 21/45 days to consider.
- 7 days to revoke/rescind after signing.

- Failing to comply with OWBPA does not invalidate the settlement agreement.
- It permits the employee to pursue his ADEA claim.
- Employer bears the burden to prove strict compliance.

Releasing Age Claims – Considerations

- Note that the statute does not create its own cause of action and does not apply to other claims (at least for most courts).
  - *Champlin v. NationsCredit, 307 F.3d 368 (5th Cir. 2002).*
  - *Branker*, 981 F. Supp. 862 (S.D.N.Y. 1997) (statute only applies to ADEA claims).
- The statute can lead to unusual results. Example: individual represented by lawyer executes a settlement; settlement does not notify the individual to secure counsel. Valid?
- There are times when you may not care about securing a valid age release.

3. Fully Resolving FLSA claims

- The Fair Labor Standards Act (FLSA) was enacted in the 1930's to protect employees from employers with disproportionate bargaining power.
- Whether and how these cases can be settled has been debated for decades. Under the law, court approval of DOL approval had been required to fully resolve wage and hour claims under the FLSA.
- Daunting challenge for employers who simply want to comply with the law. How does one settle a claim for overtime and secure peace of mind?
- Circuit split on the issue:
  - Fifth Circuit: Bona Fide Dispute Rule.
  - Other Circuits: Court or DOL Supervision.

Settling FLSA Claims in the Fifth Circuit – The "Bona Fide Dispute" Rule

- Parties may settle bona fide wage and hour disputes privately.
  - *Martin v. Spring Break '83 Productions, L.L.C.*, 688 F.3d 247 (5th Cir. 2012)(employer and employee may settle FLSA claim without court or DOL approval as long as the settlement resolves a bona fide dispute re hours/pay).
  - Case centered on a claim for unpaid wages.

Remember – Standard Release May Not Encompass Overtime Claims

- *Bodle v. TXL Mortgage Corp.*, No. 14-20224 (5th Cir. June 1, 2015).
- After settling a non-compete dispute, plaintiff executed a generic release of all claims associated with his employment.
- That did not bar him from suing for overtime.
- The generic release settling the non-compete dispute did not resolve a bona fide dispute as to overtime.

Resolving FLSA Matters Outside of the Fifth Circuit

- No private settlements of FLSA claims or, stated differently, the release may not be affected.
- Need Court or DOL supervision and approval.
- Followed in many other jurisdictions (*e.g.*, 2d, 4th, 6th, 8th, & 11th Circuits).

Cheeks v. Freeport Pancake House, Inc., Case No. 14-299-cv. (2d Cir. August 7, 2015).

- Question presented: Can parties stipulate to dismiss with prejudice FLSA claims under Fed. R. Civ. P. 41(a)(1)(A)?
- Holding: No. DOL/court must review settlement.
  - Disparate bargaining power.
  - In *dicta* noted other concerns: plaintiff's attorney fees had run amok; overbroad release; confidentiality vs. FLSA's remedial purposes, etc.

Settling FLSA Claims – Takeaways

- In Texas, parties can privately settle a wage and hour dispute, if the settlement agreement is to resolve *that dispute*.
- General releases, without more, will not bar FLSA claims.
- In Texas and elsewhere, evaluate whether representations from employee about wage hour matters will help secure peace of mind when settling employment matters.
  - Example: Employee represents that employee has reported all hours and been paid for all hours worked, etc.

4. No-Rehire Provisions – The *Golden* Rule

- Recent ruling from California throws new potential wrinkle in fully resolving employment disputes.
- Single plaintiff lawsuit by terminated employee. Files suit for discrimination. Settlement reached. As part of settlement, individual is required to agree he (or she) cannot work for employer (or its affiliates).
- Fairly standard.
- Not so fast, says the Ninth Circuit.

No-Rehire Provisions – cont'd

- *Golden v. Calif. Emergency Physicians*, No. 12-16514 (9th Cir. April 8, 2015).
- Doctor terminated from practice group.
- Sues for race discrimination.
- Settlement agreement: Physician waives his rights to employment with Defendant or any facility that Defendant may own or with which it may contract in the future.
- District court: Settlement agreement's no-rehire clause violates California's restraint of trade law, Cal. Bus. & Prof. Code §16600.

Golden (cont'd)

- California Business and Professions Code Section 16600:

  Every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void.

No-Rehire Provisions – *Golden* (cont'd)

- 9th Circuit reverses and remands.
- Remanded for factual determination as to whether the no-rehire clause "constitutes restraint of a substantial character to Dr. Golden's medical practice."
- Dissent:
  - "The court will need a Ouija board to 'find' any of the facts that the majority believes are relevant to whether the agreement will violate section 16600."

No-Rehire Provisions – *Golden* Takeaways

- No-rehire covenants can be subject to higher scrutiny in California.
- As with non-compete and other agreements, be cautious in drafting "one size fits all agreements" when representing multi-state employers.
- Bigger concern when dealing with multi-state organizations.

5. Those Pesky Taxes

- Many settlements seem to get to the issue of withholding only after the parties reach agreement on the dollar amount of a settlement.
- That often leaves an important consideration open until late in discussions.
- The following chart reflects how taxes are intended to be addressed per the IRC.

Type of Recovery	Taxable as Plaintiff's Income?	Authorities
Compensatory, actual damages, including lost wages (front or back pay)	Yes	26 U.S.C. §104(a)(2); *Commissioner v. Schleier*, 515 U.S. 323 (1995)
Compensatory damages for **emotional** distress, pain & suffering (NOT associated with personal physical injury and NOT including mental expenses from emotional distress)	Yes	26 U.S.C. §104(a)(2)
Compensatory damages for **emotional** distress, pain & suffering associated with personal **physical** injury	No	*Id.*
Medical expenses associated with **emotional** distress	No	*Id.*
Punitive damages **EVEN IF ASSOCIATED WITH PHYSICAL INJURY**	Yes	*Id.*
Liquidated damages (such as FLSA, FMLA, ADEA)	No	*Id.*; Rev. Rul. 72-268.
Costs & attorney fees	Yes	*Commissioner v. Banks,* 543 US 426 (2005)

Tax Treatment of Settlement Proceeds – Allocation

- Expressly allocate settlement proceeds up front.
- After-the-fact allocation is more susceptible to attack by the IRS.
- When a settlement agreement expressly allocates the settlement proceeds among various types of damages, the allocation is generally binding for tax purposes, as long as the agreement is entered into by the parties in an adversarial context, at arm's length, and in good faith. *See e.g.*, *Bagley v. Commissioner*, 105 T.C. 396, 406 (1995), *aff'd* 121 F.3d 393 (8th Cir. 1997).

Tax Treatment of Settlement Proceeds – Allocation (cont'd)

- Step 1: Wages?
  - Standard FICA and income tax deductions apply.
- Step 2: Otherwise Taxable?
  - 26 U.S.C. §104(a)(2) is the only way payment might not be taxable: physical injury.
  - IRS: Most employment settlements do not meet this standard; physical injury = observable or documented bodily harm (bruising, bleeding, etc.).

See IRS Chief Counsel Memorandum (October 22, 2008), *available at* http://www.irs.gov/pub/lanoa/pmta2009-035.pdf.

- Step 3: Allocate Costs and Attorney Fees?

Tax Treatment of Settlement Proceeds – Solutions

- One commonly utilized option is require that the individual indemnify the employer for tax consequences of settlement.
- Employers often do not feel this is protective enough.
- Typically involves including tax counsel/CPA in discussions. Some things are best left to professionals…