BUSINESS BRIEFS

Legal Developments Affecting Business

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Retirement Plan Alert: $35 Million Verdict Entered in Breach of Fiduciary Duty Case

By Randy Cook

A Federal District Court in Missouri recently entered a $35 million verdict against an employer and its pension committee for breaching their fiduciary duties regarding the employer's retirement plan. The court found that the fiduciaries failed to properly monitor the fees paid out of plan assets, failed to comply with the plan's Investment Policy Statement, and failed to act prudently in the selection of the investment alternatives that were offered to the participants. If you serve as a fiduciary to your retirement plan – hint: if you're an owner of your company, you *do* – then *Tussey v. ABB, Inc.* is a must read.

<u>Background</u>. Like many employers, ABB, Inc. formed a pension committee and appointed a few of its key employees to serve on the committee. The committee was charged with selecting the plan's investment advisor, selecting the plan's recordkeeper, and selecting the plan's custodian. The committee interviewed a number of providers and ended up hiring Fidelity Investments and its related companies (Fidelity Research and Fidelity Trust) to perform all three functions. This is often referred to as a "bundled plan."

The agreements that ABB entered into with Fidelity provided that Fidelity would be paid for its services almost entirely through "revenue sharing." Revenue sharing is a behind-the-scenes transfer of money from a mutual fund to a plan's recordkeeper as an incentive to include the fund on the plan's investment menu. Different mutual funds pay different percentages in revenue sharing, and some mutual funds pay no revenue sharing at all. At present, paying a plan's administrative expenses through revenue sharing is legal, but only if done properly.

<u>Mistake #1 – Failure to Properly Monitor Fees</u>. Although the court found that the total fees paid to Fidelity for administrative services may have started out as reasonable, they became unreasonable as plan assets grew. Most administrative service agreements base the cost of recordkeeping primarily on the number of plan participants, not on the size of plan assets. This makes sense because the amount of work performed by a recordkeeper typically grows as more participants are added to the plan, but it doesn't necessarily grow just because assets increase. However, under the agreement between ABB and Fidelity, Fidelity basically was being paid the *greater of* all revenue sharing generated from the mutual funds, or a minimum dollar amount. The court ruled that the pension committee had a duty to negotiate a reduction in fees from Fidelity when the total dollar amount being paid "per head" became unreasonable. Unfortunately for the committee, there was no evidence that they ever calculated the total dollar amount being paid to Fidelity for recordkeeping services, let alone negotiated for a reduction of that amount.

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Mistake #2 – Failure to Comply With Investment Policy Statement. An Investment Policy Statement ("IPS") is a document that sets forth specific guidelines that plan fiduciaries agree to follow in selecting and monitoring plan investments. Although adoption of an IPS is not required by law, many pension committees choose to go this route so that they can later prove that they have engaged in "procedural prudence" while discharging their fiduciary duties. In ABB's case, the IPS stated (among other things) that all revenue sharing would be used to reduce the cost of providing administrative services. Putting that type of clause in an IPS is appropriate when the cost of administrative services is determined by the number of plan participants. However, as indicated above, the fee charged by Fidelity for its administrative services increased as revenue sharing increased. Thus, the court ruled that even if the total dollar amount paid to Fidelity had been reasonable at all times, the pension committee violated its own IPS by allowing fees to rise as revenue sharing rose. Because an IPS is considered legally binding on the fiduciaries who create it, violation of the IPS equals *per se* breach of fiduciary duty.

Mistake #3 – Failure to Act Prudently in the Selection of Investments. Like most 401(k) plans, ABB's plan offered participants a menu of mutual funds to choose from. As indicated above, some – but not all – of the mutual funds pay revenue sharing, which reduces the employer's costs in running the plan. During the trial the court focused on a particular incident in which the ABB pension committee elected to remove a non-Fidelity fund from the platform and replace it with a Fidelity fund. Although the committee claimed that the non-Fidelity fund had been removed because its performance was "deteriorating," the committee was unable to show that it had actually reviewed the three to five-year investment performances of either the non-Fidelity fund being removed or the Fidelity fund that replaced it. What did come out at trial was the fact that the Fidelity fund paid substantially more in revenue sharing than the fund that was removed. Ultimately, the Fidelity fund underperformed the removed fund, and the court determined that the pension committee had breached its fiduciary duty to act prudently in the selection of investments.

The Lessons of *Tussey v. ABB, Inc.* The *Tussey* case offers plan fiduciaries several valuable lessons. First, if plan assets are being used to pay all or a portion of plan administration fees, review those fees at least annually to make certain that they are reasonable within the industry. Second, if your pension committee has adopted an IPS, review that IPS carefully to make certain that you are meeting the standards of care that you have set for yourself. Third, prepare pension committee minutes that carefully document the analysis that goes in to the committee's decisions to retain or remove funds. Finally, if you are working within a "bundled plan," consider unbundling it. The best-run pension committees are the ones that have independent advisors sitting at the table together, keeping an eye on each other. If you would like more information about fiduciary duties or the formation and operation of a pension committee, please contact us.

The Top 5 Ways to Discourage Your Former Employee's Attorney
By Randall Sutton

Employers often feel that they don't have the upper hand when dealing with employment claims. Employment laws can feel quite one sided. For employers dealing with difficult employee relations issues, there are really only two ways to "win."

- Best Case: The company and the current or former employee work things out, and the employee never feels that he or she needs to consult with a lawyer.
- Next Best: The unhappy current or former employee visits a lawyer, and the lawyer has absolutely no interest in taking the case.

If a lawyer takes the case and files a lawsuit, even though the company may ultimately prevail, even getting the case dismissed or obtaining a favorable verdict won't feel like much of a "win" after all the time and energy expended. It's much better to avoid court altogether.

Remember, in most employment cases, the employee's attorney only gets paid if the employee wins. If there isn't the potential for recovery, or if the attorney will need to work too hard for too little reward, most savvy plaintiff attorneys won't take the case. So how does an employer discourage unnecessary litigation? Here are the five most effective tools:

#1 - Document Before you Discharge

Sugar-coating is tasty on breakfast cereal, but it has no place in a performance review. It's only fair to give your employees constructive feedback and an opportunity to improve. Juries are more apt to like the employer who bent over backwards to treat the employee fairly. An employee who fails to heed repeated written warnings will not be sympathetic. Make sure employees are clear about the consequences of substandard performance. An employee who sees the writing on the wall will react to a termination far differently than an employee who is taken by surprise. Ruin the opposing attorney's day by giving your employee every chance to succeed before making a discipline or termination decision.

#2 - Investigate Employee Complaints

Employee complaints that go unaddressed are fertile ground for lawsuits. If your employee complains, especially about harassment, wages, working conditions, or other matters of consequence, you need to give investigation and response your highest priority. Grievances can quickly fester and grow. The longer a problem goes unaddressed, the more difficult it will be to cure. It the employee doesn't feel that the company is satisfactorily responding, the odds are good that he or she will talk to a lawyer about taking action.

When investigating the complaint, don't jump to conclusions. Conduct a thorough and fair investigation. Document every step. Then make an impartial decision based upon the evidence. As your reward, here is the best news . . . you don't need to be right! So long as you carefully investigate the complaint and take balanced and appropriate action to prevent future problems, your decisions should hold up in court.

#3 - Understand and Follow Wage and Hour Rules

Wage and hour laws defy common sense. Moreover, the laws give very little wiggle room, making wage claims difficult to defend. The laws frequently reward undeserving employees for small technical violations. An employer's good intentions are irrelevant. Wage and hour laws are complicated too, with lots of exceptions . . . and exceptions to those exceptions.

Your employee's attorney knows how hard it is for you to comply with these technical requirements. Rather than having sympathy, the lawyer knows that even if the termination of his or her client was otherwise lawful and trouble-free, small violations of the wage and hour laws could still bring a successful outcome. An unhappy employee who goes to see an attorney for any reason will likely end up in a conversation about the wage and hour practices of the employer. To avoid these claims, the key is to obtain a legal audit of your wage and hour practices *before* there is a problem, making sure that your pay practices will hold up under close scrutiny.

#4 - Up-to-Date Personnel & Supervisor Manuals

Remember when only ear lobes were pierced? Remember when you had to drive to work to check your email? Remember when Facebook and other social media didn't exist, and there was simply no effective way to announce to the world a person's every thought or movement? If your personnel manual was last updated in "those days," then it is long out of date.

Every year, new laws are enacted and courts put twists on old laws. The way in which we work likewise changes fast enough that policies can quickly become outdated. In a lawsuit, you need to prove compliance with the law and that you follow best practices. An out of date manual, one that doesn't comply with the law, or worse yet, a manual that doesn't reflect how you do business, can cause more trouble than not having one at all.

We recommend that our clients also provide a "supervisor handbook" giving detailed instructions about how to carry out the company's personnel policies. Think of the personnel manual as the "rule book." The supervisor handbook explains how to play the game. In addition to being a great tool, the supervisor handbook is evidence in court about how hard you are working to make sure that your team complies with employment laws.

#5 - Training

It used to be that training was just a really good idea. Now, it's a minimum requirement. Recent court cases have held that your personnel manual and good intentions mean nothing if you don't train your employees. All employees should periodically receive harassment & discrimination training. Moreover, managers and supervisors can either be the cure for or the source of your greatest liabilities. To avoid claims, managers and supervisors need to be trained in issues such as family leave compliance, ADA, wage and hour laws, and effective documentation.

These five steps are important in discouraging a plaintiff attorney from taking on your employee or former employee's case. They also just might make your company even more effective in managing its employee relations. If your company would benefit from updated policies or a wage and hour compliance audit, please contact us.

Members of LLCs Face Added Exposure for Workers' Compensation Claims

By Steve Hitchcock

The Oregon Court of Appeals recently issued a decision of importance to owners of limited liability companies that have employees. In *Cortez v. Nacco Materials Handling Group, Inc.*, the Court held that the exclusivity provision of the Oregon Workers' Compensation Law did not apply to members of an LLC. This means that even if an injured employee of an LLC obtains benefits under the workers' compensation system, the employee can still sue the members of the LLC if their negligence caused the employee's injury.

Cortez

Cortez was injured by a forklift owned by his employer and obtained benefits for the injury under a workers' compensation claim. Cortez also sued the member of the LLC alleging that the member committed negligence in the implementation of safety policies. The member defended the claim by arguing that the exclusive remedy for an injured worker falls under the Workers' Compensation Law. Oregon Revised Statute 656.018 states that the remedy obtained by an injured worker under a worker's compensation claim is exclusive as to the employer and its "employees, officers and directors." In other words, if you are injured and receive benefits from a workers' compensation claim, you cannot then sue the employer, another employee, the officers or directors of the employer for the same injury. The Court of Appeals, however, noted that the legislature did not include "members" or "managers" in the exclusive remedy statute. Accordingly, an injured worker *can* sue an LLC's members or managers for their own negligence in causing workplace injuries, even if the injured employee receives a workers' compensation benefit for the injuries.

LLCs v. Corporations

The ruling in *Cortez* would be different if the employee worked for a corporation rather than a limited liability company. Corporations are owned by shareholders that elect directors. The directors appoint officers who run the day-to-day operations of the corporation. The statutory framework of LLCs is a little less formal and more flexible. There are two types of LLCs—member-managed and manager-managed. Member-managed LLCs are controlled by the members (who act as the equivalent of officers of corporations). In a manager-managed LLC, the manager (who often is a member, but does not have to be) controls the day-to-day operations of the LLC. If an officer or director of a corporation commits negligence resulting in a workplace injury and the injured worker obtains benefits from a workers' compensation policy, the worker is barred from suing the officer or director. However, if the employer is an LLC, and the member or manager commits negligence resulting in injury, the employee can sue the member or manager, even after receiving a workers' compensation benefit.

Protecting Your Business After *Cortez*

What does this mean for employers? While there are a number of factors to consider when choosing a type of business entity, the *Cortez* decision may provide additional incentive to consider forming a corporation rather than an LLC, especially if your business will have any employees.

Additionally, owners of existing LLCs with employees should talk to their insurance agents about the business' coverage and whether any adjustments should be made. Since this case eliminated statutory protection for members of LLCs from workers' compensation claims, the question becomes whether alternative insurance might be available to a member sued by an employee of the LLC for alleged negligence, which resulted in the employee's on the job injury. Most operating companies have comprehensive general liability (*"CGL"*) insurance policies. Those policies generally extend coverage to an accident resulting in bodily injury or property damage, to which the insured may have some liability. Unfortunately, the CGL policy has several exclusions which may be problematic.

Coverage is excluded for any obligation of the insured for liability under any workers' compensation or disability benefits law. Even situations in which the insured is a non-complying employer under the state workers' compensation statute, i.e., the employer did not obtain workers' compensation insurance, the insured is not covered under a CGL policy for the liability incurred to an employee as a result of the non-compliance with the statute.

Another provision in the CGL Policy excludes coverage for bodily injuries sustained by an employee of the insured arising out of and in the course of employment or while performing duties relating to the conduct of the insured's business.

However, these exclusions may be nullified by the separate insurance provision of a CGL policy. That standard policy requires that the insurance be applied to each named insured separately. Typically, in CGL policies, the members of an LLC are also named insureds. As a result of the separate insured's provision, a member sued by an employee of the LLC may be able to avoid application of the workers' compensation employee exclusion by arguing that, as to the member, the injured person was not his or her employee and thus the exclusions are irrelevant. In discussing this matter with Mr. Ed Davis of Maps Insurance, he felt that such an argument might be successful. However, Mr. Davis recommended that any LLC with employees should contact their insurance agent and seek a letter opinion from the insurance company confirming that the member will, in fact, have coverage under the CGL policy in the event of an employee injury claim.

If you or your clients have any questions about the ramifications of the *Cortez* decision, please contact our office.

Facebook and the Internet in Hiring: A Tool or Time Bomb?

By Jennifer Paul

As an employer, you may have noticed a string of Associated Press releases and news articles reporting that employers are asking – or requiring, depending on the story – job applicants to provide their Facebook passwords. The reports stirred-up significant media speculation regarding the legality of such hiring practices and invasion of privacy concerns.

Facebook even entered the fray, making several public statements explaining that although it had no immediate plans for litigation against specific employers, it would support legislative policy and stakeholders seeking to ban such practices. Facebook also stated that giving out Facebook login information violates the social network's terms of service. In late April, Representative Eliot Engel (NY) and Jan Schakowsky (Illinois) introduced draft legislation to the House of Representatives banning employers from asking current and potential employees for access to private social networking accounts. This draft legislation, called the Social Networking Online Protection Act (SNOPA), includes civil penalties in amounts up to $10,000.00 for violations of the Act. The Senate continues to work on its own version of similar legislation, led by Senator Richard Blumenthal (Connecticut), an early public proponent for policies banning the use of social media in hiring.

Employers ask us all the time: Can you ask job applicants to show their Facebook page? What if online content is not password protected? Can I Google applicants and review information posted publically? In the face of these questions, the better question is: *Do you really want to*?

I know the temptation to get the information is strong. The internet is a potential gold mine in evaluating whether an applicant is the right fit for the long haul. Who wouldn't want to know if their next sales associate acts inappropriately in social settings? Or, shouldn't an employer run a quick Google search to verify that the applicant's resume is accurate? What about learning that the applicant just got a big settlement check after suing his last employer?

<u>Legal Risks</u>

However, keep in mind that once you get certain information, you can't "unring the bell." Employers can't discriminate in hiring based on a laundry list of factors, including (but certainly not limited to) age, sex, national origin, sexual orientation, disability, status of a whistleblower in a previous job, and pregnancy.

When you view an applicant's Facebook page or Google them, you don't get to pick and choose what information you're exposed to. After an online search, you may learn a lot more than you bargained for, and some of that information may be legally protected. Once you know that information, what are you going to do with it?

Another risk employers take with online searches of applicants is that the information learned may not be accurate. How can we be certain that the information is correct? Or whether the person being discussed online is even the applicant you are interviewing?

Now, what if you decide not to hire that applicant? Your reasons for not hiring may be innocent, legitimate, and have nothing to do with information you found online. Maybe there was a more qualified applicant or the person interviewed poorly. But, once you've seen the legally protected information, you've opened the door for the applicant to become a plaintiff, because it will be difficult to prove that you didn't take that information into account in the hiring decision.

Finally, applicants can argue that an employer's requirement to provide a Facebook password is a violation of federal law. The Stored Communications Act prevents access to password protected sites without authorization. To make a claim under the Act, an applicant would have to successfully argue that the employer coerced the password from the applicant. That kind of claim would be difficult for an applicant to prevail on, but if the applicant won, the employer could be on the hook for compensatory damages, punitive damages and attorney fees.

<u>How to Conduct Online Searches</u>

As a best practice, we recommend that you act carefully before screening applicants online. As discussed above, an employer exposes itself to potential liability when conducting online searches in the hiring process. The absolute safest and most conservative approach is to step away from the computer when vetting applicants.

If you must screen applicants online, make sure you can justify the online search for the specific job you are hiring. Not all positions will warrant an online search. Take a close look at the job description for the position you are hiring and determine if any legitimate job related reasons for screening the applicant exist.

If you have legitimate job related reasons for screening applicants online, make sure to have a policy in place that helps to mitigate potential liability associated with the practice. Make sure the policy addresses these concerns:

- what online information is relevant to the hiring process;
- how the information found online will be used;
- what will be done with unwanted information or information unrelated to the job;
- at what point in time during the hiring process will the research occur; and
- whether or not the online research will be stored.

Once a policy is in place, apply it consistently to all applicants. It is also recommended that the person conducting the online research be someone independent from the hiring process so that only relevant job related information is forwarded to the decision makers. That person should have very clear instructions about what should and should not be shared with the hiring decisionmaker.

Overall, it is important to determine whether your company would benefit from utilizing online search methods in its hiring practices. If these online searches will help your company find the best employees, you should implement a clear policy in order to protect your business from related challenges. Saalfeld Griggs can help you put a hiring policy in place and assess other issues in your workplace surrounding social media. Give us a call or send us an email.

FIRM SEMINARS AND ANNOUNCEMENTS

Thank you to everyone who voted for us in the **Statesman Journal's "Best of the Mid-Valley"** competition. We are excited to announce that Saalfeld Griggs received the Gold Medal for best mid-valley law firm for the second year in a row. This is a great honor and we appreciate the community's support.

David E. Myers and **Kara M. Cogswell** have recently joined Saalfeld Griggs PC. David received his B.S. in Political Science at Brigham Young University. He graduated *magna cum laude* from Willamette University College of Law in 2011 and was an Associate Editor on the Law Review. He recently attended the University of Washington School of Law's Graduate Program in Taxation where he earned a Master of Laws (LL.M.) in Taxation. He is joining the Business and Taxation Practice Group. **Kara M. Cogswell** graduated from the University of Oregon with her B.A. in journalism in 2002. She went on to study at Willamette University College of Law and also graduated in 2011. She will be working in the Employee Benefits & Executive Compensation Department. Welcome David & Kara!

Saalfeld Griggs PC is a proud sponsor of the **Oregon Artist Series Foundation**, which is currently showing 'Sculpture Now' in the sculpture garden at the Salem Conference Center.

Hunter Emerick presented a Marion County Bar Association Litigation Skills Seminar on May 16th. His presentation was entitled "Practicalities and Strategies for Motion for Summary Judgment Practice," and was attended by Marion County attorneys.

The Oregon Society of CPAs will be hosting their Estate & Trust Conference on June 22nd in Portland. **Bob Saalfeld** and **Jeff Moore** will be speaking about the $5 Million Lifetime Gift-Tax Exclusion. Visit the Oregon Society of CPAs' Estate & Trust Conference page for more information.

The staff and attorneys at Saalfeld Griggs recently gave up a Saturday to volunteer for **Habitat for Humanity** by assisting in the building of a house in south Salem. We are very proud to have helped a deserving family in our community.

Salem-Keizer Education Foundation Board of Directors recently appointed **Steve Hitchcock** as Treasurer. Salem-Keizer Education Foundation is a catalyst for enhancing the education of Salem-Keizer public school students by providing resources for creative and innovative programs and materials, education and mobilizing the community and sustaining collaborative partnerships that supports its goals.