

*MARYLAND STATE BAR ASSOCIATION*  
*SECTION OF LABOR AND EMPLOYMENT LAW*  
**NEWSLETTER**

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Albert W. Palewicz, *Editor*

**Section Officers:**

Peter D. Guattery, *Chair*

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Jonathan R Krasnoff, *Recording Secretary*



**FROM THE CHAIR**

**By Peter D. Guattery**

On April 1st, the Supreme Court handed down the much anticipated decision in *14 Penn Plaza LLC v. Pyett*, 200 U. S. 321 (2009). The Supreme Court found that a broad arbitration provision in a collective bargaining agreement which included a specific agreement to arbitrate statutory discrimination claims was fully enforceable. The Court decision split 5-4, with Souter, Stevens, Ginsburg and Breyer in the minority. The case arose in the context of ADEA claims asserted by a group of security guard employees following their reassignment to jobs as porters and cleaners. The District Court and the Court of Appeals for the Second Circuit refused to compel arbitration, holding that *Alexander v. Gardner-Denver, Co.*, 415 U.S. 36, forbids enforcement of collective bargaining provisions requiring arbitration of ADEA claims. *14 Penn Plaza LLC* obviously represents a significant shift in favor of arbitration of statutory discrimination claims, and is recommended reading for all of us.

The Section will meet this coming June at the Maryland Bar Association's Annual Meeting in Ocean City. This year's meeting will feature an interactive informational session on the practicalities of trying an employment case from both the Plaintiff and Defense perspective, and will include a jury of peers to critique and comment on the case and the lawyers. Join us for this interesting presentation – "Think Like a Juror Not Like A Lawyer – Trying An Employment Case Before A Jury." Check your Bar newsletter for information on meeting time and location.

Finally, thank you also to Semmes, Bowen & Semmes in Baltimore for providing the articles for this edition of the Newsletter with their valuable commentary on our area of practice.

*Peter D. Guattery*

**EDITOR'S CORNER**

**By Albert Palewicz**

This edition contains fewer articles than we usually have, but it probably contains more information than usual, as well. There are two articles that deal with difficult, complicated, and critically important issues. As a result these articles are both much longer than we usually attempt. The first deals with the area of employer and attorney liability under newly enacted Medicare provisions regarding third-party insurers and their attorneys in workers' compensation cases. The other concerns the drafting, interpretation, and enforcing of restrictive covenants in employment agreements in Maryland. Both articles are well written and exhaustive. Those who practice in any of the involved areas will find the information very useful, I believe.

There is also an article on the proposed Employee Free Choice Act, newly introduced in Congress for this term. The author presents the proposed legislation from both points of view, management and labor. If you are not already familiar with the proposals of the Employee Free Choice Act, this will be of interest to you.

The Baltimore attorneys of Semmes- Bowen & Semmes prepared the articles for this issue. They worked with Don Burke as coordinator for the issue. We thank them for their excellent work.

The next issue, to be issued just before and distributed at the Summer Meeting of the Maryland State Bar Association in Ocean City, will be prepared by the attorneys at the law firm of Gary Gilbert and Associates in Silver Spring, MD. Gary will act as coordinator of the issue.

The Section took part in a Brown Bag lunch sponsored at the NLRB's Baltimore Regional Office on March 23. About 35 section members were present, and the discussion was lively and prolonged. Regional Director Wayne Gold answered questions about what the Region anticipates over the next year in budget and staffing. There was also discussion about what

*(continued on page 2)*



**EDITOR'S CORNER (continued)**

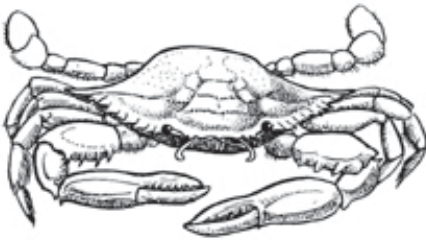
the NLRB might do in the event of the passage of some or any parts of the Employee Free Choice Act now pending in Congress. No one can predict what will be enacted, if anything, but if something does make it into law this year, there will be changes for the NLRB and for those who practice before it.

The Section Council will be meeting to plan the Spring Dinner meeting, and to finalize the program for the Summer Meeting in Ocean City. Anyone who has suggestions for the Council concerning any of its programs, may contact Section Chair Peter Guattery or any member of the Council.

We will see you all in Ocean City!

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MARYLAND STATE BAR ASSOCIATION ANNUAL MEETING  
OCEAN CITY, MARYLAND  
JUNE 10-13 2009



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## ARTICLES

# Restrictive Covenants in Employment Agreements in Maryland

By James A. Johnson

One thing I've learned as a trial lawyer is that there are no sure things in litigation. When I first graduated from law school, I agonized over whether to estimate the chances for success in a case at 70% or 75%. Now, I know that there are only three choices: about even; a little better than even; and a little less than even.

While this degree of uncertainty may be acceptable among litigants, it is problematic when it comes to advising clients about restrictive covenants in employment agreements. When an employee resigns or is fired, both the employee and the former employer deserve a clear description of their rights and obligations. Only with a clear delineation of rights and obligations can the employee, the former employer and the new employer conform their actions to the law, enjoy their own rights and respect each other's rights.

Unfortunately, the enforceability of an employer-employee restrictive covenant rests on an imprecise standard: i.e. whether the particular restriction in the particular circumstance is "unreasonable." While the enforceability of most written contracts is determined on a more objective standard (the plain meaning of the words of the agreement), a restrictive covenant is treated differently because it is a restraint of trade which restricts, albeit temporarily, a person's freedom to compete with certain customers or in certain territories. Under Maryland law, "A person may not . . . by contract, combination, or conspiracy with one or more persons, unreasonably restrain trade or commerce . . ." Md. Code Ann., Commercial Law Article, §11-204(a)(1) (emphasis added). Therefore, a restrictive covenant will not be enforceable unless it constitutes a reasonable restraint.

As a result of this reasonableness standard, instead of a clear statement as to whether a covenant is enforceable, the courts only offer comments such as:

- a. It depends on whether under all the circumstances of each particular case, the restrictions are reasonable to protect the employer's legitimate interests, do not impose an undue burden on the employee and do not unnecessarily impact the

public interest;

- b. The restriction must be reasonably limited in geographic scope but, in a particular case, might encompass the whole nation or the whole world;

- c. The restriction must be reasonably limited in time but, depending on the facts of the particular case, three years might be okay or one year might be too long; and

- d. The court might delete portions of the contract or even rewrite the provisions.

Such uncertainty regarding the enforceability of restrictive covenants creates a quagmire for both employers and employees. Reliance on a restrictive covenant may create a false sense of security and lead an employer to forego available safeguards to backup customer contacts and to protect confidential information. Further, the employer's post-employment decision whether to pursue enforcement in the courts is complicated by the reality that one court might find the covenant enforceable under one set of circumstances while another court might find the very same covenant unenforceable under other circumstances.

From the former employee's perspective, uncertainty as to the enforceability of a restrictive covenant serves only to exacerbate the force of the restraint by preventing the employee from knowing exactly what he can do and placing a cloud over his ability to work for another employer within his skill set. Who wants to hire a potential lawsuit?

## BACKGROUND

Given the degree of uncertainty, it might be helpful to review how we got here.<sup>1</sup>

In the Middle Ages, English courts found all restraints on trade to be void and unenforceable, including post employment covenants not to compete.<sup>2</sup> Skill in a trade was the vital factor in economic status and was obtainable only through apprenticeship. The guild system permitted a man to work only in the trade in which he was apprenticed and membership in a guild was not easily attained. Travel was difficult and strangers were not welcome. If a man couldn't work at his trade in his hometown, he could hardly work at all.<sup>3</sup> If a master and apprentice entered into a restrictive covenant, the apprentice would not be able to practice his craft following the apprenticeship.<sup>4</sup> Craft guilds attempted to restrict competition through these covenants but courts showed an unwillingness to enforce them.<sup>5</sup>

It was in this background that when, in 1415, the celebrated Dyer's Case, the earliest known case of a contractual restraint of trade, came before the judge, he became so enraged by an attempt to restrain a dyer from working in a town for just a half year that

he cursed the deal void: "By God, if the plaintiff were here he should go to prison until he paid a fine to the king."<sup>6</sup>

By the early eighteenth century, English courts began issuing decisions which allowed limited restraints on trade. Thus, in *Mitchel v. Reynolds* (1711),<sup>7</sup> an English court upheld an agreement in which a baker assigned the lease of his shop and promised not to practice his trade in the same parish for the duration of the lease. The *Mitchel* decision established a new framework for analyzing restrictive covenants and ushered in the application of what became known as the "rule of reason" test for evaluating restrictive employment contracts. Although the traditional rule remained that restraints on trade were facially invalid, the courts allowed for reasonable exceptions.<sup>8</sup>

By the Nineteenth Century, the "rule of reason" test was modified to include balancing the interests of the parties with the interests of the public.<sup>9</sup> In *Horne v. Graves* in 1831,<sup>10</sup> the English court found that the element of reasonableness was not limited only to the consideration stated in the contract, but also its potential impact on the public welfare.<sup>11</sup> Horner concluded that, if a restrictive covenant within an employment agreement was likely to cause undue injury to the public, then the covenant should be found unenforceable.

#### DEVELOPMENT IN THE UNITED STATES

The development of the law of covenants not to compete in the United States mirrors English common law. Many state courts began to adopt the "rule of reason" test and the proposition that the law upholds restraints on trade if the restraints are (1) reasonable under the circumstances;<sup>12</sup> (2) ancillary to a valid transaction or relationship;<sup>13</sup> and (3) limited in duration and geographic scope.<sup>14</sup>

#### DEVELOPMENT IN MARYLAND

The modern day law of restrictive covenants in Maryland traces its roots to the decision of the Court of Appeals in *Silver v. Goldberger* in 1963.<sup>15</sup> That case involved a non-compete for two years with a fifty-mile, geographic limitation. The two departing employees opened their competing employment agency two blocks away. The Court held that enforceability depends on whether the restriction is "justified" or "unjustified."

According to the Court, a restriction is justified when a part of the compensated services of the former employee consisted in the creation of the good will of customers and clients which was likely to follow the person of the former employee.

By contrast, the Court held that a restriction is not justified if the harm is merely that, through his work and experience, the employee has become a more efficient competitor.

In 1965, the Court of Appeals addressed a salesman of ten-pin pin setters in *MacIntosh v. Brunswick*.<sup>16</sup> The former employee notified Brunswick that he had taken a position with the Bowl-Mar Company. Brunswick withheld payment of an earned bonus and sued the employee. The Court held the restriction unenforceable because there was no geographic restriction.

The next decision appeared in 1968 in *Tuttle v. Riggs-Warfield-Roloson, Inc.*<sup>17</sup> Contrary to the *MacIntosh* decision, the Court, in *Tuttle*, issued an injunction based on a two-year restriction which had no geographic restriction. The restriction there was as to customers of the employer. The scope, customers of the employer, was considered to be a sufficiently narrow limitation so as to replace the requirement of a geographic limitation.

After he left Riggs-Warfield, Tuttle, an insurance agent, sold a policy to a customer with whom he had had close personal ties while employed at Riggs-Warfield. This action spurred the injunction.

By 1967, the Court of Appeals developed the basic statement of enforceability which continues today. In *Ruhl v. F. A. Bartlett Tree Experts Co.*, the restriction was for two years in five Eastern Shore counties and a contiguous county in Delaware.<sup>18</sup> The Court upheld the restriction. The Court's description of the law gives virtually no assurance to an employer or former employee who wants to understand its/his/her rights.

This Court has had a number of cases involving the validity of restrictive covenants in a contract of employment. Covenants of this nature are in restraint of trade; the test is whether the particular restraint is reasonable on the specific facts. The general rule in Maryland, as in most jurisdictions, is that "restrictive covenants in a contract of employment, by which an employee as a part of his agreement undertakes not to engage in a competing business or vocation with that of his employer on leaving the employment, will be sustained 'if the restraint is confined within limits which are no wider as to area and duration than are reasonably necessary for the protection of the business of the employer and do not impose undue hardship on the employee or disregard the interests of the public.'" There is no arbitrary yardstick as to what protection of the business of the employer is reasonably necessary, no categorical measurement of what constitutes undue hardship on the employee, no precise scales to weigh the interest of the public. The decisions in this State and in other jurisdictions are helpful, but as in so many other fields of the law, the determination must be made on the particular circumstances.

One can only imagine an attorney giving this explanation to an employer or former employee.

The decision in *Ruhl* was particularly harsh because the employee had worked with Bartlett since he was 14. He had only a high school education, had a family to support, and the only business he knew was the tree business.

In 1972, in *Gill v. Computer Equipment Corp.*, the Court of Appeals again approved a restrictive covenant with no geographic limitation.<sup>19</sup> There the employer was a manufacturer's representative. The two-year restriction was a restriction on doing business with any manufacturer which had been represented by the employer's division in the year immediately preceding the employee's discharge.

In 1973, the Court of Appeals summarized the law of restrictive covenants in *Becker v. Bailey*.<sup>20</sup> There the Court declined to enforce a restrictive covenant limited in time (two years) and geographic scope (D.C. and three Maryland counties) because the employee was an unskilled worker who provided no unique services and had no particular contact with customers. The Court provided guidance every bit as helpful as that in *Ruhl* and concluded:

While such restrictions may be enforced under some circumstances, there is no sure measuring device designed to calculate when they are. Rather, a determination must be made based on the scope of each particular covenant itself; and, if that is not too broad on its face, the facts and circumstances of each case must be examined. When such an analysis is made, some restrictive covenants are deemed enforceable while others are not. Maryland follows the general rule that restrictive covenants may be applied and enforced only against those employee who provide unique services, or to prevent the future misuse of trade secrets, routes or lists of clients, or solicitation of customers. *Ruhl v. Bartlett Tree Co.*, supra. . .

However, in 1973, the wheels began to come off the cart in *Millward v. Gerstung*.<sup>21</sup> Millward, a well-known operator of sports camps, was restricted from running camps for two years in Baltimore City and surrounding counties. Millward was not trained by the employer, had no confidential information of the employer and had no ongoing contact with prospective customers. Nevertheless, the Court enforced the restriction because of Millward's unique reputation and qualifications even though that reputation and qualifications had preceded the employment.

In the early 1990's, things really got out of hand from the perspective of a lawyer looking for guidance to advise the employee and the employer as to their rights. *Halloway v. Faw Casson &*

*Co.*, concerned an accounting firm.<sup>22</sup> The contractual restriction provided that, if, within the next five years, a departing accountant did work for any of the firm's clients, the accountant must pay the firm an amount equal to the firm's billings to the client for the previous twelve months, regardless of whether the accountant had any prior contact with the client. Apparently, the aspect which troubled the Court was the lengthy restriction against servicing clients with whom Halloway had had no contact while he was employed by Faw Casson. The Court of Special Appeals held that it could re-write the contract by charging the duration from five years to three years.<sup>23</sup>

The Court of Appeals reviewed some prior decisions.

Appellate courts in Maryland have addressed a large number of covenants not to compete and upheld varying temporal restrictions. See, e.g., *Millward v. Gerstung Int'l Sports Educ., Inc.*, 268 Md. 483, 302 A.2d 14 (1973) (two year prohibition against engaging in sports camp business upheld); *Gill v. Computer Equip. Corp.*, 266 Md. 70, 292 A.2d 54 (1972) (two year prohibition against serving customers of division of computer company upheld); *Tuttle v. Riggs-Warfield-Roloson*, 251 Md. 45, 246 A.2d 588 (1968) (two year restriction on employee of insurance general agency upheld); *Ruhl v. F.A. Bartlett Tree Expert Co.*, 245 Md 118, 225 A.2d 288 (1967) (two year prohibition against competition by area manager of tree care company upheld); *Western Maryland Dairy, Inc. v. Chenowith*, 180 Md. 236, 23 A.3d 660 (1942) (six month restriction on milk route salesperson held reasonable); *Griffin v. Guy*, 172 Md. 510, 192 A. 359 (1937) (restrictive covenant between barbers upheld although unlimited as to time); *Tolman Laundry, Inc. v. Walker*, 171 Md. 7, 187 A. 836 (1936) (one year restriction on employee of laundry business upheld); *Anderson v. Truitt*, 158 Md. 193, 148 A. 223 (1930) (sale of furniture business with twenty-five year restriction on competition held reasonable); *Deuering v. City Baking Co.*, 155 Md. 280, 141 A. 542 (1928) (three month restriction on employee of bakery upheld); *Geurand v. Dandeleit*, 32 Md. 561 (1870) (sale of dyeing and scouring establishment and lease of premises which prevented seller, lessor from competing upheld although unlimited as to time). Cf. *Food Fair Stores, Inc. v. Greeley*, 264 Md. 105, 285 A.2d 632 (1972) (forfeiture clause in employee pension plan prohibiting competition was unreasonable because it contained no limitation as to area or duration); *Tawney v. Mutual Sys. of Md.*, 186 Md. 508, 47 A.2d 372 (1946) (two year prohibition on competition by small loan manager held unreasonable).

Without addressing or reversing the duration as re-written by the Court of Special Appeals, the Court of Appeals engaged in its

own form of contract re-drafting, holding that the restriction was severable on a client-by-client basis: issuing an injunction as to some clients but not as to others.

The mischief continued in 1991 with *Fowler v. Printers II, Inc.*<sup>24</sup> There, the one-year restriction prohibited solicitation of both any actual customer of Printers and any potential customer to whom Printers had submitted a bid, even if the departed employee had never heard of the customer or the previous bid. The Court held that it could simply blue-pencil the offending language (prospective customers) and enforce the restriction only as to customers with whom the employee had dealt.

So, where are we now? To be enforceable, a restrictive covenant must be reasonably limited in duration. In some cases, a three year limitation might be acceptable, while, in other cases, one year would be too long.

The restriction must also be sufficiently limited in a geographic scope. But, in some cases, a world-wide restriction might be acceptable.

If the restrictive covenant is not sufficiently limited in duration and scope, it is not enforceable, unless, of course, the Court decides to rewrite the contract.

Further, the enforceability of a restrictive covenant depends on an analysis of the reasonableness of the restriction under all of the circumstances.

If you were a really good employee and contributed unique services to your former employer, you are more likely to be bound by the restriction.

But wait, it gets even more nebulous.

In *Deutsche Post Global Mail, Ltd. v. Conrad*, the Court refused to enforce the restrictive covenant because there was so little competition and the employer had such a large share of the market.<sup>25</sup> However, in *United Rentals, Inc. v. Davison*, the Court refused to enforce the non-compete because there were many competitors and the employer had a negligible share of the market.<sup>26</sup>

In *Hekiman Laboratories, Inc. v. Domain Systems, Inc.*, the Court enforced a broad, worldwide restriction against a defendant who the Court believed had not been honest in his testimony.<sup>27</sup> In *Deutsch Post Global Mail Limited*, the Court refused to enforce a strikingly similar covenant in the case of former employees who had met with the employer and disclosed the fact that they were opening up a competing business.

Thus, it appears, that one important factor is whether the judge

approves of the employer's or employee's post-employment conduct. A few examples make the point:

§ *MacIntosh v. Brunswick*: Employee meets with the employer and discloses the plan to compete . . . restriction held unenforceable.

§ *Becker v. Bailey*: Former employee avoided working for customers of former employer . . . restriction not enforceable

§ *Heikman v. Domain*: The Court believed that the employee gave false testimony . . . restriction enforced.

§ *Deutsch Post Global Mail v. Conrad*: Employee meets with employer and discloses intent to compete . . . restriction held unenforceable.

While these principles might be appropriate in the context of litigation, they play absolute havoc with the ability of the employer and former employee to understand their rights and obligations prospectively.

In sum, restrictive covenants provide valuable protection to an employer's business. However, the squishy and uncertain unenforceability of restrictive covenants can cause more harm than good. If the courts were unable to provide more definitive guidance concerning enforceability, then the Maryland legislature might consider following California and declaring that restrictive covenants in employment agreements generally are unenforceable. What would happen? Perhaps:

- a. The playing field between employer and employee would be leveled so that powerful employers could no longer force on employees a contract of adhesion with severe restrictive covenants;
- b. Employers and employees would have a clearer understanding of their post-employment rights;
- c. Employers would realize that they would have to solidify customer relationships because they could not restrict departing employees;
- d. An employee would be free to leave his employment without fear of being banished from the career he knows;
- e. Job opportunities for former employees would not be restricted by prospective employers' fears of stepping into a lawsuit;
- f. Employers would be free to hire valuable employees without fear of a costly and time-consuming lawsuit from a former employer;
- g. Customers would benefit from the increased competition if the former employee and the employer both solicit the business actively; and
- h. Employers would still have protection for true trade secrets and confidential information, including customer lists and customer information, through Maryland's version of the Uniform Trade Secrets Act.<sup>28</sup>

From the various court decisions, attorneys, employers and employees can divine general principles in their predictions of the enforceability of restrictive covenants. However, the ambiguities and generalities of court analyses leave such considerations in the realm of predictions and estimates. Except in the most egregious situations, it is difficult to predict whether a court would enforce a particular restriction against a particular former employee in the particular circumstances. This may be the best that can be achieved from court decisions addressing a “reasonable” standard. While action declaring employee restrictive covenant unenforceable generally may help all parties to achieve relative certainty, this would probably require legislative action and could only apply prospectively.<sup>29</sup>

Footnotes:

<sup>1</sup> I extend my profound thanks to Kevin Cox, an associate with Semmes, Bowen & Semmes, for his invaluable help in researching and explaining the development of the law of restrictive covenants in English courts.

<sup>2</sup> Harlan M. Blake, Employee Agreements Not to Compete, 73 HARV. L. REV. 625, 629 (1960).

<sup>3</sup> *Arthur Murray Dance Studios of Cleveland v. Witter*, 105 N.E.2d 685 (Ohio Com.Pl. 1952).

<sup>4</sup> *Id.* The indenture contract common in the era of guilds required the apprentice to refrain from competing with the master for a specified period of time after the completion of training. In the few cases which raised the issue, the courts consistently held that restraints restricting the right to work were unlawful. These cases are usually cited for the proposition that the common law originally treated all restraints as violating the principle of economic freedom and therefore void. *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> Y.B. 2 Henry 5, fol. 5, pl. 26 (1414); *see also* Minda, *supra* note 6 (discussing Dyer's Case as the first reported case involving contractual restraint of trade).

<sup>7</sup> *Mitchel v. Reynolds*, 1 P. Wms. 181 (Q.B. 1711).

<sup>8</sup> *Mitchel*, *supra* note 12 at 248, 251-52.

<sup>9</sup> *Id.* at 366.

<sup>10</sup> 131 Eng. Rep. 284 (C.P. 1831)

<sup>11</sup> *Id.* (holding that a 100 mile restriction imposed on a dentist apprentice was unreasonable because the personal nature of dental services made it impossible for such a wide area to be serviced by only the previous employer himself).

<sup>12</sup> *See, e.g., Oregon Steam Navigation Co. v. Winsor*, 87 U.S. (20 Wall.) 64 (1874). In order for a noncompetition agreement “to be reasonable, the promisee must have an interest worthy of protection;” therefore, such a restraint must “be subsidiary to an otherwise valid transaction or relationship that gives rise to such an interest.”

<sup>13</sup> *See Blake*, *supra* note 1, at 630-31, 637-46.

<sup>14</sup> *See Pyke v. Thomas*, 7 Ky. (4 Bibb) 486, 488 (1817); *Pierce*

*v. Woodward*, 23 Mass. (6 Pick.) 206, 206-08 (1828) (sale of grocery store with verbal agreement not to compete within certain distance); *Palmer v. Stebbins*, 20 Mass. (3 Pick.) 188, 193 (1825) (exclusive agreement to carry all goods of obligor and not encourage competition with boatman to carry goods); *Pierce v. Fuller*, 8 Mass. 223, 225 & n.[a] (1811) (purchase of stage line between Boston and Providence, Rhode Island); *Nobles v. Bates*, 7 Cow. 307, 309 (N.Y. 1827).

<sup>15</sup> *Silver v. Goldberger*, 231 Md. 7 (1963).

<sup>16</sup> *MacIntosh v. Brunswick*, 241 Md. 24 (1965).

<sup>17</sup> *Tuttle v. Riggs-Warfield-Roloson, Inc.*, 251 Md. 45 (1968).

<sup>18</sup> *Ruhl v. F. B. Bartlett Tree Expert Co.*, 245 Md. 118 (1967).

<sup>19</sup> *Gill v. Computer Equipment Corp.*, 266 Md. 170 (1972).

<sup>20</sup> *Becker v. Bailey*, 268 Md. 93 (1973).

<sup>21</sup> *Millward v. Gerstung Int'l Sport Educ.*, 268 Md. 483, 302 A.2d 14 (1973).

<sup>22</sup> *Halloway v. Faw Casson & Co.*, 319 Md. 324 (1990).

<sup>23</sup> *Halloway v. Faw Casson & Co.*, 78 Md. App. 205 (1989).

<sup>24</sup> *Fowler v. Printers II, Inc.*, 89 Md. App. 448 (1991).

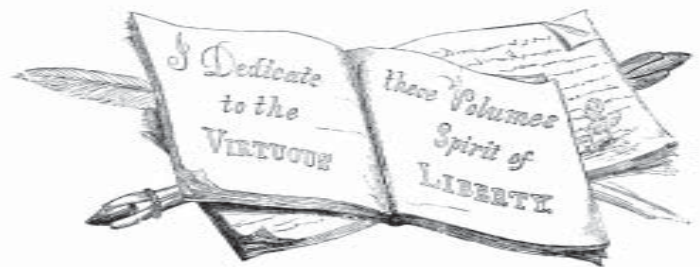
<sup>25</sup> *Deutsche Post Global Mail, Ltd. v. Conrad*, 292 F.2d 748 (D.Md. 2003).

<sup>26</sup> *United Rentals, Inc. v. Davison*, 2002 WL 31994259 (2002).

<sup>27</sup> *Heikman Laboratories, Inc. v. Domain Systems, Inc.*, 664 F. Supp. 493 (S.D. Fla. 1987) (applying Maryland law).

<sup>28</sup> Md. Code Ann., Commercial Law Art., §11-1201 *et seq.*

<sup>29</sup> The doctrine of *stare decisis* would limit an action by Maryland's Court of Appeals to reverse its field on the issue. Further, any legislative enactment would apply on prospectively because of the prohibitions on *ex post facto* laws and laws impairing the obligation of contracts. *See, e.g.,* United States Constitution, Article I, Section 10.



# The Employee Free Choice Act- Redux

By Donald F. Burke

On the morning of Thursday, March 10, 2009, for the third time in as many years, a pair of companion bills was placed in the Congressional hopper. Together they are designated as H.R. 1409 and S. 560. The bills constitute an amendment to the National Labor Relations Act designated the Employee Free Choice Act of 2009 (“EFCA”).<sup>1</sup> These will be two of the most closely watched bills pending in the 111th Congress because there has been a change this year in the political landscape.

In summary, the EFCA “streamlines” procedures for employees to decide on union representation and bargain a first contract. Under the EFCA, as presently drafted, a union would be automatically recognized in a workplace when a majority of employees sign cards stating that they want to be represented by that union. Under current labor law, the National Labor Relations Board will certify a union as the exclusive representative of bargaining unit employees by secret ballot election, which is held if more than 30% of the employees in a bargaining unit sign cards asking for representation by a union. Pursuant to the EFCA, a union can demand that an employer begin bargaining within ten days of certification of the union as the exclusive bargaining representative for an appropriate unit of employees as a result of the majority card check provision. A majority is 50% of the employees plus one is styled “majority sign-up.” In the event that the union and employer cannot agree upon the terms of a first collective bargaining contract either the union or management can request the assistance of the Federal Mediation and Conciliation Service (“FMCS”). If the FMCS mediator is unable to reach a “deal” within an additional thirty (30) days, the dispute will go to binding interest arbitration and the results of the arbitration will be imposed on the parties for two years.

Additionally, the EFCA imposes much stiffer penalties against employers – not against unions - for discrimination in their anti-organizing efforts. These sanctions include increased civil penalties, injunctive relief, and up to three (3) times the back pay if an employee is discharged or discriminated against during an organizing campaign. Finally, the bill provides for civil penalties of up to \$20,000.00 per violation against employers who are found to have willfully or repeatedly violated employees’ rights during an organizing campaign or first contract drive.

President Obama has signaled his intention to sign the EFCA

into law once it reaches his desk. However, in 2007, the Democrats lacked the majority in the Senate to avoid filibuster and to ensure its passage. Democrats also lacked the majority in the Senate in 2008. Of course, as mentioned above, the political landscape, particularly in the Senate, changed after the 2008 election and the inauguration of President Obama. This means that the EFCA has a good chance of becoming law. The question remains: How will the final bill shape up and will there be compromise on some of the more radical provisions of the EFCA? What is undeniable is that this bill has polarized labor and management more than any other piece of legislation since the original National Labor Relations Act (“NLRA”) to which this is an amendment was enacted into law in 1935 as an integral part of President Roosevelt’s new deal legislation. It is both helpful and insightful to visit the National Labor Relations Board’s (NLRB) website to read that, “Congress enacted the National Labor Relations Act in 1935 to protect the rights of employees and employers, to encourage collective bargaining and to curtail private sector labor and management practices, which can harm the general welfare of workers, businesses and the U.S. economy.”<sup>2</sup>

Because the EFCA legislation would materially change the NLRA, it has engendered much controversy and debate from both sides of the labor bar. Organized labor posits two primary arguments in support of the EFCA. First, unions assert that the NLRB representational procedures are broken; and therefore, are easily abused by employers seeking to delay and frustrate employee rights. Unions argue that the penalties for committing unfair labor practices during the course of an election, including promises of benefits, and threats of reprisals or discharge, are small compared to the overall effect such actions have on election results. Second, unions argue that current NLRB law is ineffective to redress break-downs in negotiations given the heavy burden of proof on unions to establish bargaining violations in initial contract cases and the lack of effective remedies. The unions argue that these inadequacies continue to be exploited by employers to avoid reaching agreement before the expiration of the certification year and to eventually encourage already frustrated employees to vote in favor of decertification in some instances.

Organized labor has made the EFCA its top legislative priority. One need only look at the Service Employees International Union (“SEIU”) website<sup>3</sup> to readily observe the priority given to the passage of the EFCA by this strong union. The website states: “One million strong for Employee Free Choice Act.” It also states

A robust middle-class. Economic Growth and Shared Prosperity. The American Dream. None are possible

unless workers have the free choice to bargain for a better life - in their workplaces and in our nation. That's why SEIU members need the Employee Free Choice Act - critical legislation that would restore workers' freedom to form unions and bargain for better wages, health care, and working conditions – and have a voice in our economy. We're going to show the new president and Congress that there are one million people who want to give hard working families a chance to get ahead. Can you be one of the first?

Another web page on the SEIU site shows a management financed and produced “movie” on YouTube where the union focuses on a recent management statement that “our country is on the verge of ‘armageddon,’ ‘nuclear war,’ and ‘the demise of civilization.’” The SEIU website further states that “According to CEOs and their front groups, the fabric of our nation may well fall apart, all because of the Employee Free Choice Act. Its opponents no longer debate the merits of the bill, and instead resort to hyperbolic vitriol intended to inflame the public and press. In reality, the Employee Free Choice Act is a bipartisan, common sense economic recovery for working families that will pump billions into our nation’s economy.”

In an article by Isaiah J. Poole,<sup>4</sup> published shortly after the EFCA passed in the House of Representatives in 2007, he wrote, “The report (a Canadian report comparing secret ballot elections to majority-sign-up election systems in several provinces) estimates that if EFCA became law, union membership would increase by about 10% - thus increasing the pool of workers who are more likely to get access to employee-paid health insurance and retirement benefits that are substantially more prevalent among unionized workers than they are among non-unionized workers.” He also quotes Senator Tom Harkin, Democrat from Iowa, who says, “By passing the Employee Free Choice Act and giving workers a seat at the table, we can start to reverse these negative trends (declining union membership). Union participation in the workplace means everybody wins. When employees have voice - when they can ask for better wages and benefits and make suggestions about how to do things better - employers benefit too.”

Finally, the SEIU website cites from a recent address by the President to the AFL-CIO on March 3, 2009, in which the President states: “I have every confidence that if we are willing to do the difficult work that must be done, we will emerge from these trials stronger and more prosperous than we were before. And as we confront this crisis and work to provide health care to every American, rebuild our nation’s infrastructure, move toward a clean energy economy, and pass the Employee Free Choice Act, I want you to know that you will always have a seat at the table.”

The management oriented members of the bar have expressed serious concerns over the EFCA, and in particular, its vaguely defined parameters. In management’s view, EFCA will not give effect to true employee choice but actually eradicate that choice, which is embodied in the secret ballot election. Management describes the Employee Free Choice Act as intentionally “mis-named.” In a report published by the Heritage Foundation,<sup>5</sup> James Sherk and Paul Kersey write

The Act would replace the current system of secret-ballot organizing elections with card checks, in which workers publicly sign union cards to organize and join a union... under the EFCA, once organizers collect signed cards from a majority of the company’s employees, all of the company’s workers would be forced to join the union without a vote. This strips workers of both their fundamental right to vote and their privacy. Both union and the employer would know exactly which workers want to join the union, leaving workers vulnerable to threats and intimidation... when workers decline to sign the union card on the spot, union organizers return again and again to pressure these holdouts to change their minds.

Under the card check system, instead of holding the traditional secret ballot election, which has stood the test of time for over seventy (70) years, a company’s employees can become unionized if just 50% plus one (1) of the employees in an appropriate unit signs union pledge cards. If passed, the NLRB will draft model pledge card language and procedures to establish the validity of signed cards. Many employers have publically stated their objection to this provision of the proposed Act. In fact, during the week of March 8, 2009, industrialist/investor Warren Buffet, an early Obama supporter, stated in a CNBC interview that “I prefer to retain the right to vote in privacy.”

Another major flaw asserted by management with the EFCA concerns the mandatory arbitration provisions. Critics have noted that binding arbitration is at odds with long-standing principals of self-determination that are the underpinnings of capitalism in the private sector. Unlike the public sector, private sector employers and employees have at their disposal economic weapons, such as the lock-out and strike, to achieve their respective bargaining objectives. What becomes of these rights should the parties be forced into binding arbitration? Further, the same critics object to the lack of any defined standards the arbitrator must apply in making its determination at arbitration. The question remains open if the arbitrator will defer to standards that exist in the public sector (which are not necessarily appropriate for the private sector) or whether these “standards” will be amorphous, leading to inconsistent rulings and decisions – thus making the entire

# Recent Cases Offer Employment Discrimination Protection to Transgender People

By Christina Bolmarcich

venture an even bigger gamble for management. The Heritage Foundation noted in its report that in states like Michigan that do use binding arbitration, it takes an average of fifteen months for arbitrators to make a ruling. Moreover, an arbitrator's ruling would be final. Workers could not appeal a decision that gave them too little pay and the employer could not appeal a decision that would bankrupt the company. Also, while only management is usually accused of discharging workers for organizing on behalf of a union for employees, employers decry the bill's provision which ignores union abuses during organizational campaigns but rather increases penalties on employers alone.

It is a safe bet to conclude that some version of the EFCA will pass either this year or within the next three years. It is also worthy of note that irrespective of the EFCA, in the last three years in contested union elections, unions have won a majority of those elections for the first time since 1978. It seems that the fortunes of the unions are on an upswing, even without the EFCA. Finally, it is entirely conceivable that there may be compromises for the sake of political expediency if the EFCA is to become law. This is mainly due to an odd consortium of several Republicans and certain "Blue Dog Democrats," such as Pennsylvania's Republican Senator Arlen Specter, who often vote with the Republicans on conservative matters especially in the U.S. Senate. These so called Blue Dog Democrats are mainly from southern states which, for example, have given huge subsidies to non-union foreign auto production plants and other non-union facilities. Therefore, even with the significantly changed political landscape in Washington, there still may not be enough Senate votes to force cloture and thereby enact a compromise bill even during an activist Obama administration. What will a compromise, if any, look like? Will it substitute a three quarters vote for 51 percent of the vote? Will it soften employer only penalties? Will it amend or lessen the impact of binding arbitration? Only time will tell.

Footnotes:

<sup>1</sup> There were 40 Senate co-sponsors and 223 House co-sponsors for the companion bills. In 2007, the measure had 46 co-sponsors in the Senate and 230 co-sponsors in the House.

<sup>2</sup> See National Labor Relations Board (last visited March 16, 2009) <[http://www.nlr.gov/about\\_us/overrun/national\\_labor\\_relations\\_act](http://www.nlr.gov/about_us/overrun/national_labor_relations_act)>.

<sup>2</sup> See Service Employees International Union (last visited March 16, 2009) <<http://www.seiu.org>>.

<sup>4</sup> Isaiah J. Poole, Campaign for America's Future: How Free Choice Act Aids Workers (last modified May 1, 2007) <<http://www.ourfuture.org/blog-entry/how-free-choice-act-aids-workers>>.

<sup>5</sup> James Sherk and Paul Kersey, How the Employee Free Choice Act Takes Away Workers' Rights, The Heritage Foundation, June 20, 2007.

**Transgender:** A person having personal characteristics (such as transsexuality or transvestism) that transcend traditional gender boundaries and corresponding sexual norms.<sup>1</sup>

**Transsexual:** A person who strongly identifies with the opposite sex and may seek to live as a member of this sex especially by undergoing surgery and hormone therapy to obtain the necessary physical appearance (such as by changing the external sex organs).<sup>2</sup>

Many metropolitan areas are beginning to enact ordinances, codes, and general laws to extend unlawful discrimination protection in employment to persons considered transgender and transsexual. According to the Transgender Law & Policy Institute, nationally, ninety-three (93) cities and counties have enacted laws prohibiting discrimination based on gender identity and gender expression.<sup>3</sup> These laws offer an added protection beyond Title VII of the Civil Rights Act of 1964, which only forbids employment discrimination on the basis of race, color, religion, sex (gender), and national origin.<sup>4</sup>

Historically, courts and legislative bodies have been reluctant to offer protection to transgendered and transsexual employees. Only presently is the Maryland State Assembly considering legislation that would broaden the protections afforded to transsexual and transgender public employees. This legislation, S. Res. 566 (Md. 2009) and H. Res. 474 (Md. 2009), proposes to include the term "gender identity" for the purposes of prohibiting discrimination with regard to public accommodations, housing, and employment.<sup>5</sup> The proposed legislation does not seek to amend The Maryland Annotated Code of 1957, Article 49B, Maryland Commission on Human Relations, Section 16, Unlawful Employment Practices, which is directed at providing protection to all employees, and fails to include the term "gender identity." Md. Ann. Code Art. 49B § 16 (2003).

By way of local progressive example of extending protection to transgender and transsexual employees, the Baltimore City Code, Article 4, Community Relations Commission, Subtitle 3, Unlawful Practices, Subsection 1, Employment, provides:

Except where a particular occupation or position requires, as an essential qualification, the employment of a person or persons of a particular race, color, religion, national origin, ancestry, sex, age, marital status, physical or mental capability, or gender identity or expression and that qualification is not adopted by means of circumventing the purposes of this article, it is an unlawful practice to: (1) for any employer to discriminate against an individual with respect to hire, tenure, promotion, terms, conditions, or privileges of employment or any matter directly or indirectly related to employment.

*Baltimore City, Md., Code, Art. 4, § 3-1(1)* (Feb. 28, 2009).<sup>6</sup>

Recently, a number of state administrative and court decisions have provided significant support and protection for transgender and transsexual employees. The following decisions demonstrate a marked trend in the direction of protecting transgendered and transsexual employees and highlight the continuous political struggle to provide equal rights to all employees regardless of their sexual orientation, gender identity, and gender expression.

**Massachusetts:** In *Robert Lie, also known as Allie Lie, v. Sky Publishing Corporation*, 15 Mass. L. Rptr. 412, 2002 WL 31492397 (Mass. Super. Ct. 2002), the Superior Court of Massachusetts found that a male-to-female transsexual could maintain an action for unlawful discrimination based upon sex (gender), sexual orientation, disability, and retaliation.

In this case, the plaintiff, Lie, a biological male, suffered from “gender dysphoria,” a gender identity disorder.<sup>7</sup> In 1994, Lie was employed by the defendant, Sky Publishing Corporation (“Sky”), as an editorial assistant. Subsequent to her employment at Sky, Lie began to take hormones in response to her diagnosis of gender dysphoria. In May 1998, Lie began to wear “traditional female attire to work.” *Id.* at 1. Sky’s management personnel then met with Lie and requested that she “only wear traditional male attire while at work.” *Id.* She refused. In July 1998, Lie was discharged under the pretext that she violated Sky’s e-mail policy and had exhibited workplace hostility.

As part of the court’s opinion as to whether Lie had valid employment discrimination claims against Sky, it first discussed at length the differences between “transgendered individuals” and “transsexuals.” *Id.* The court stated that a “‘transgendered individual’ is also a distinct umbrella term used to describe any individual who exhibits a gender identity that does not conform to societal expectations, including transsexuals, transvestites, and others who engage in gender expression that is different from that associated with their biological sex.” *Id.* citing Kristine W. Holt, *Reevaluating Holloway: Title VII Equal Protection and the*

*Evolution of a Transgender Jurisprudence*, 70 Temp.L. Rev. 283, 290 (1997). A transsexual is a person born a male or female and whose physique “mark” that individual as male or female yet, in spite of the biology, the person is compelled, mentally and emotionally, to live as a member of the opposite gender. *Id.* (additional citations omitted).

The court found that Lie had alleged sufficient facts to establish that she was a transsexual. The court then analyzed whether she had a valid claim for unlawful discrimination based upon sex (gender), sexual orientation, disability, and retaliation under Mass. General Laws Chapter 151B that warranted the denial of Sky’s motion for summary judgment. The court divided its analysis into four parts.

First, it tackled the issue of discrimination on the basis of sex (gender) in violation of Mass. General Law Chapter 151B. Because this was a case of first impression, it heavily relied on the decisions in *Price Waterhouse v. Hopkins*, 490 U.S. 228, 235 (1989) and *Enriquez v. West Jersey Health System*, 342 N.J. Super. 501, 515, 777 A.2d 365 (N.J. Super. Ct. App. Div. 2001).

In *Price Waterhouse, Hopkins*, a woman, was employed as a senior manager by a nationwide professional accounting firm. When evaluating Hopkins for partnership, her supporters praised her abilities. However, a number of her evaluators criticized her interpersonal skills. Several of her evaluators commented that she was too masculine. She was denied partnership. She then resigned and brought an action against the accounting firm in the U.S. District Court for the District of Columbia. Her lawsuit asserted unlawful employment discrimination on the theory that her evaluations had been based on sexual stereotyping. The District Court held the firm liable under that theory, as it found that (a) the firm and its partners had not intentionally discriminated on the basis of gender, but (b) the firm had consciously maintained an evaluation system influenced by sex (gender) stereotypes. On certiorari, the U.S. Supreme Court held that an employer commits actionable discrimination when it relies upon sex (gender) stereotypes in any decision making process concerning employees.

The court then referred to *Enriquez v. West Jersey Health Systems* regarding the application of discrimination laws to transsexuals. The *Lie* court, quoting the *Enriquez* court, observed that “It is incomprehensible to us that our Legislature would ban discrimination against heterosexual men and women; against homosexual men and women; against bisexual men and women; against men and women who are perceived, presumed, or identified by others as not conforming to the stereotypical notions of how men and women behave, but would condone discrimination against men or women who seek to change their anatomical sex because they

suffer from a gender disorder. We conclude that sex discrimination under the [state's anti-discrimination statute] includes gender discrimination so as to protect plaintiff from gender stereotyping and discrimination for transforming herself from a man to a woman." Enriquez, 342 N.J. Super. at 515. Using the New Jersey Court's interpretation of the legislative intent and the U.S. Supreme Court's finding in *Price Waterhouse*, the Court found that Lie's claim for sex (gender) discrimination was sufficient to survive summary judgment where Lie had presented evidence that Sky's conduct was based on stereotypical notions of gender.

Second, it discussed the issue of discrimination based on a disability. The Court pointed to its analysis of gender identity disorder and noted that the disorder is listed in the diagnostic manual of the American Psychiatric Association, and that it is "arguably physical or mental impairment." DSM-IV at 533. Lie alleged that this disorder, in its unmitigated form, substantially limited her in the major life activities of working, relating to others, and caring for oneself. The Court found that the DSM-IV supported Lie's contention. The Court agreed with Lie and found that she had established a *prima facie* case of disability discrimination.

Third, it discussed whether Lie had a viable claim as to sexual orientation discrimination. The Court found that she could not establish this claim since she failed to present sufficient facts to support her claim that Sky terminated her based on her actual or perceived sexual orientation.

Fourth, the Court found that Lie has a meritorious claim for retaliation since Sky was aware of a pending claim by Lie with the Massachusetts Commission Against Discrimination at the time it discharged her. The Court stated that "Knowledge of the filing with the Commission creates an issue of material fact for the jury as to whether the plaintiff's termination was an act of retaliation based upon knowledge." *Lie*, 2002 WL 31492397 at 8.

**New York:** Using the same analytical construct as the *Price Waterhouse* Court, the Court in *Caillean McMahon Tronetti v. TLC Healthnet Lakeshore Hospital*, 2003 WL 22757935 (W.D.N.Y. 2003), relied on the U.S. Supreme Court's finding that

Title VII barred not just discrimination based on the fact that [plaintiff] was a woman, but also discrimination based on the fact that she failed to 'act like a woman' - that is, to conform to socially-constructed gender expectations. [*Price Waterhouse*]. What matters, for purposes of this part of the *Price Waterhouse* analysis, is that in the mind of the perpetrator the discrimination is related to the sex of the victim: here, for example, the perpetrator's actions stem from the fact that he believed that the victim was a man who failed to act like one. Thus, un-

der *Price Waterhouse*, 'sex' under Title VII encompasses both sex - that is, biological differences between men and women - and gender.

*Id.* at 4.

The Court found that the plaintiff, Tronetti, a transsexual, could maintain a Title VII claim for alleged employment discrimination based on his employer's perceptions of male and female gender roles with respect to Tronetti's inability to "act like a man." *Tronetti*, 2003 WL 22757935 at \*4. In support of the Court's finding, it stated that "[t]ranssexuals are not gender-less, they are either a male or a female and are thus protected under Title VII to the extent that they are discriminated against on the basis of sex." *Id.*

**Pennsylvania:** The Third Circuit denied defendant's motion to dismiss in *Danny Lee Mitchell v. Axcan Scandipharm, Inc.*, 97 Fair Empl. Prac. Cas. (BNA) 960, 2006 WL 456173, (W.D. Pa. 2006) on the grounds that Mitchell, a preoperative transsexual, diagnosed with general identity disorder, presented sufficient evidence demonstrating that Mitchell's failure to conform to certain societal gender stereotypes regarding how a man should act and look was sufficiently pled. It also noted that discrimination, based on societal notions of gender was prohibited pursuant to the U.S. Supreme Court's decision in *Price Waterhouse*.

**New Jersey:** The United States District Court for the District of New Jersey found that a transsexual employee stated a valid claim when he sued the Atlantic County for harassment that he alleges he endured while he was employed at The Atlantic County Justice Facility. In *DePiano v. Atlantic County, et al.*, 2005 WL 2142972 (D.N.J. 2005), DePiano sued the defendants pursuant to the New Jersey Law Against Discrimination ("LAD") claiming, *inter alia*, that he was subjected to a hostile work environment based on his preference for cross-dressing<sup>8</sup> outside of work.

The court looked to *Lehmann v. Toys 'R' Us, Inc.*, 626 A.2d 445 (N.J. 1993) for the standard necessary to establish a claim for a hostile work environment under LAD. The *Lehman* court found that a successful claim involves establishing four elements: "[T] he complained-of conduct (1) would not have occurred but for the employee's gender; and it was (2) severe or pervasive enough to make a (3) reasonable [person] believe that (4) the conditions of employment are altered and the working environment is hostile and abusive." *Id.* at 453.

The *DePiano* court found that the "cumulative effects of frequent taunting" because of the revelation of "one of his embarrassing secrets," subjected the plaintiff to "severe and pervasive harass-

ment” in the workplace. As such, DePaino’s claim for harassment survived summary judgment. *DePiano*, 2005 WL 2142972, at 9.

**Florida:** The Florida Commission on Human Relations (“Commission”) issued two recent opinions championing the rights of the transgendered under state law. The first opinion was issued in the 2004 matter of *Connie Fishbaugh v. Brevard County Sheriff’s Dept.*, FCHR Order No. 04-103 (Fl. Comm. Human Rel. 2004). In *Fishbaugh*, the Commission found that the petitioner, a transsexual employee, had a viable state claim for discrimination based on transsexuality rather than strictly based on sex (gender). This finding was consistent with the U.S. Supreme Court’s opinion in *Price Waterhouse*.

The second opinion was issued in the 2006 matter of *Madalynn A. Shepley v. Lazy Days RV Center, Inc.*, FCHR Order No. 06-016 (Fl. Comm. Human Rel. 2006). In *Shepley*, the Commission found that the respondent discriminated against the petitioner, in violation of state law, when it fired her. The Commission applied the *Price Waterhouse* analysis and reasoned that although the employer made several accommodations to facilitate the employee regarding her gender reassignment, the employer discriminated against her by terminating her without a legitimate, non-discriminatory business reason.

### Conclusion

The aforementioned cases and legislation demonstrate the shift towards expanding the current protections afforded to transgender and transsexual individuals. The protections once offered based on strict notions of biological gender are being replaced by protections offered regardless of gender but solely based on discriminatory acts against individuals in the workplace.

### Footnotes:

<sup>1</sup> *Merriam-Webster Online Dictionary* (retrieved March 4, 2009) <<http://www.merriam-webster.com/dictionary/transgender>>.

<sup>2</sup> *Merriam-Webster Online Dictionary* (retrieved March 4, 2009) <<http://www.merriam-webster.com/dictionary/transsexual>>.

<sup>3</sup> Transgender Law and Policy Institute, *Non-Discrimination Laws That Include Gender Identity and Expression* (last updated September 2007 and retrieved March 4, 2009) <<http://www.transgenderlaw.org/ndlaws/index.htm>>.

<sup>4</sup> The Civil Rights Act of 1991 (Pub. L. 102-166) (“CRA”) and the Lily Ledbetter Fair Pay Act of 2009 (Pub. L. 111-2) amends several sections of Title VII. In addition, section 102 of the CRA amends the revised statutes by adding a new section following section 1977 (42 U.S.C. §1981), to provide for the recovery of compensatory and punitive damages in cases of intentional violations of Title VII, the Americans with Disabilities Act of 1990, and section 501 of the Rehabilitation Act of 1973.

<sup>5</sup> The legislation proposes defining “gender identity” as “gender-

related identity, appearance, expression, or behavior, of an individual regardless of the individual’s assigned sex at birth,” and proposes adding the term to The Annotated Code of Maryland, State Government, Sections 20-101, 20-302, 20-304, 20-402, 20-501, 20-602, 20-603, 20-605, 20-606, 20-607, 20-702, 20-704, 20-705, 20-707, 20-1103 and State Personnel and Pensions, Section 2-302. The amendments are collectively aimed at “prohibiting discrimination based on gender identity with regard to public accommodations, housing, and employment” on the basis of “gender identity.”

<sup>6</sup> The Baltimore City Code defines “gender identity or expression” as “an individual’s having or being perceived as having gender-related self-identity, self-image, appearance, expression, or behavior, whether or not those gender-related characteristics differ from those associated with the individual’s assigned sex at birth,” *Id.* at Art. 4, §1-1(l-l).

<sup>7</sup> American Psychiatric Association, *Diagnostic and Statistical Manual of Mental Disorders, Fourth Edition*, (“DSM-IV”) at 533 (1994).

<sup>8</sup> Merriam-Webster Online defines cross-dressing as “the wearing of clothes designed for the opposite sex.” *Merriam-Webster Online Dictionary* (retrieved March 4, 2009) <<http://www.merriam-webster.com/dictionary/cross-dressing>>.



# The Medicare Secondary Payer Program and Recent Statutory Changes Effective July 1, 2009: The Days in Which Workers' Compensation Attorneys Can Ignore Medicare's Interests Have Ended

By Shiva Z. Kashani

It is no secret that the federal government has been concerned for some time about the burden of its Medicare program. In fact, Medicare has long been a growing concern. As a result of increased health care costs and a shortage of funds, Congress continues to seek methods to recoup payments for medical treatment and prescription drugs that should not be paid by Medicare.

Workers' compensation attorneys have, for more than fifty (50) years, had the responsibility to consider liabilities imposed by the Medicare Secondary Payer program ("MSP"). The federal MSP statute is constantly changing and affects all workers' compensation parties, including claimants, insurers, attorneys, and even consultants. The laws are so encompassing that they impose liability on noncompliant insurers and attorneys representing both claimants and insurers.

The most recent amendment to the MSP statute imposes mandatory reporting requirements and accompanying penalties for noncompliance, effective July 1, 2009. These requirements now make it impossible to disregard Medicare's interests in the resolution of workers' compensation claims. Workers' compensation attorneys, representing either claimants or employers, can no longer afford to overlook Medicare's interests in the resolution of claims and must exhibit less eagerness to cost-shift liability for a claimant's future medical treatment onto Medicare.

The MSP statute provides the federal government with cost-cutting measures and heavy-handed collection tools to monitor claims made by Medicare beneficiaries and to determine which of these beneficiaries remain entitled to medical treatment and prescription drug coverage first under workers' compensation insurance, also known as the "primary plan."

Workers' compensation insurance only becomes a primary payer when a Medicare beneficiary's medical treatment and prescrip-

tion drug needs are causally related to a work-related injury or illness. This includes claimants who have received workers' compensation settlements, awards, judgments, or, as the regulations provide, "other payments."

All parties in workers' compensation cases, including claimants, insurers, attorneys, and consultants, continue to have significant responsibilities under the MSP statute to protect Medicare's interests when resolving cases that may include future medical expenses. The newly enacted amendments endeavor to enforce those responsibilities by imposing hefty penalties, at the astounding rate of \$1,000.00 per day, for each claim involving an unreported Medicare beneficiary claimant. These new mandatory reporting provisions have effectively ended the days in which workers' compensation parties may have been able to afford non-compliance with the MSP program.

## BACKGROUND OF THE MEDICARE SECONDARY PAYER PROGRAM

Congress established the Medicare program in 1965 by enacting Title XVIII of the Social Security Act to provide federal health insurance for hospital and medical coverage to persons age 65 and older, certain disabled individuals, and individuals with permanent kidney failure. *See* 42 U.S.C. § 1395, *et seq.*

Medicare has been a secondary payer to workers' compensation benefit payments since the inception of the Medicare program in 1965. The MSP provisions were enacted in the early 1980s and have been modified many times since. The Centers for Medicare and Medicaid Services ("CMS"), formerly known as the Health Care Financing Administration, is a federal agency, which is part of the Department of Health and Human Services. CMS is responsible for the oversight of the Medicare program.

Due to the MSP statute's many and frequent changes since its inception, and the long road of exhausting administrative remedies, the federal appellate courts have not had many opportunities to interpret issues arising out of the statute. Most of the issues are resolved prior to appellate court review. Furthermore, the previously limited resources of CMS to completely enforce the provisions of the MSP statute have worked in the favor of noncompliant parties.

As granted by the MSP statute, Medicare can avoid disbursing payments that should be made under a primary insurance plan. Section 1862(b)(2) of the Social Security Act precludes Medicare from paying a beneficiary's medical expenses when payment has been made or can reasonably be expected to be made under a workers' compensation plan. 42 U.S.C. § 1395y(b)(2)(A)(ii).

Medicare may, however, pay for an expense when the availability

of workers' compensation insurance is unknown or prompt payment under such coverage is not expected. In that case, Medicare may make "conditional payments" when prompt insurance payment is not expected. *See* 42 U.S.C. § 1395y(b)(2)(B)(i). A conditional payment is defined as a Medicare payment made due to lack of knowledge of other coverage. 42 C.F.R. § 411.22.

If such a conditional Medicare payment is made, CMS may seek reimbursement from the insurer or from one who receives payment from the insurer, if the insurer is responsible for the expense. *See* 42 U.S.C. § 1395y(b)(2)(A)(ii); 42 C.F.R. § 411.22. If reimbursement is not made, CMS has standing to bring action against the insurer or the recipient of a workers' compensation payment. *See* 42 U.S.C. § 1395y(b)(2)(A)(iii); 42 C.F.R. § 411.24.

CMS may waive its rights in the best interests of Medicare. *See* 42 U.S.C. § 1395y(b)(2)(A)(v); 42 C.F.R. § 411.28. CMS may waive reimbursement for conditional payments made, for example, if a third party liability insurer is also liable for a beneficiary's medical treatment and prescription drugs. However, this waiver can only be obtained through prior approval of a settlement from CMS.

When a worker makes a workers' compensation claim, doubt may exist regarding the compensability of the workers' compensation claim and the causal relationship of the claimed medical expenses. The workers' compensation insurer may question whether the worker's injury or illness arose out of and in the course of his employment or whether the medical expenses are a result of the injury or illness. Such questions may be litigated, but often they are settled. The resulting settlement is likely to affect Medicare's responsibility to pay for the worker's medical expenses.

Another important provision of the MSP statute is Medicare's disregard for an admission of liability. CMS considers a workers' compensation insurer a primary payer if and when the insurer disburses payment on a claim. This remains true regardless of language contained in the settlement agreement denying liability or coverage.

So long as a workers' compensation insurer continues to carry liability for medical benefits, Medicare is relieved of responsibility as a primary payer. But if the workers' compensation settlement limits or eliminates the duty of the workers' compensation insurer to pay future medical benefits, Medicare is becomes the primary payer and is responsible for the payments.

As a result of this shift of responsibility, claimants and insurers have always had a tempting incentive to structure their settlement agreements in a way that transfers liability from the insurer to Medicare. Claimants consider this cost-shifting as an advantage

because they can keep a greater amount of the settlement funds for themselves, rather than agreeing to have a portion of the funds set-aside to pay for future medical expenses. The lump sum settlement amount will be paid directly to the claimant, rather than held in a trust or annuity pending future medical treatment.

Insurers consider the cost-shifting as an advantage because once the workers' compensation plan is no longer liable for future medical benefits, Medicare's role will change from secondary payer to primary payer. This will lead to Medicare paying for a claimant beneficiary's future medical treatment. The costs of creating a trust or annuity are also avoided.

No matter the settlement amount, all parties to workers' compensation claims continue to carry the responsibility of considering Medicare's interests. The perceived incentive to shift the cost of future medical treatment onto Medicare can result in a settlement that is unfair to Medicare.

Another example of cost-shifting is if a portion of the settlement amount is allocated for lost wages and another portion is set aside to for future medical benefits. The claimant in this example seeks to divide the funds in a way so that he will not have to use the entire settlement amount for future medical benefits. Instead, when the allocated amount for future medical expenses set aside in the agreement are exhausted, the claimant will seek further medical treatment under Medicare.

CMS is aware of the different ways in which parties attempt to shift costs, and strives to limit its exposure for injuries or illnesses which are causally related to a workers' compensation claim. To avoid the resulting subsidization by Medicare in cases of cost-shifting, the provisions of the MSP statute permit CMS to refuse to recognize a workers' compensation settlement. *See* 42 C.F.R. § 411.46(b)(2). Medicare, in the case of an unrecognized settlement, would not pay for medical benefits that should have been covered by the workers' compensation insurance plan.

If and when Medicare pays for medical treatment causally related to a workers' compensation claim, prior to realizing a primary plan must cover the costs, CMS has standing to demand reimbursement for the conditional payments made. CMS has standing to demand reimbursement from either the workers' compensation insurer or from anyone who has received a portion of the settlement funds.

On the other hand, if the workers' compensation settlement agreement is sent to CMS and CMS approves it in advance, all parties are relieved of liability for medical expenses beyond what is provided for in the agreement. Clearly, obtaining CMS approval prior to a settlement is the most favorable course of action, save the resulting costs of obtaining the approval and the associated

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delays in the settlement process.

The new legislation affecting workers' compensation insurers, as of July 1, 2009, will equip CMS with the information it needs to seek reimbursement for many claims not previously reported or approved. CMS will have notice of all primary payers who continue to carry responsibility for current Medicare beneficiaries' medical benefits.

CMS will presumably compare the electronic data submitted by the primary payers to its own information regarding each beneficiary's current treatment status. The medical diagnosis and treatment codes will be compared and CMS will easily and quickly have the capability to determine if it is disbursing payments from Medicare funds for medical benefits that should be made by the workers' compensation insurer.

The most controversial effect of the MSP statute, some attorneys contend, is the liability imposed upon the attorneys who have not protected Medicare's interests in the past. CMS has indicated the reporting requirements will be retroactive. Workers' compensation attorneys on both sides of workers' compensation cases will be well-advised to seriously consider both the liabilities imposed upon themselves and their clients by the MSP statute. And, these attorneys should then take the initiative to review cases in which they may have overlooked Medicare's interests and determine their clients' treatment or payment status.

#### TWO TYPES OF SETTLEMENT AGREEMENTS

To understand the liability imposed by the MSP statute, we must first understand the difference between the two types of settlement agreements recognized by CMS. It is important to note a settlement may have characteristics of both types of agreements, and liability exists, as always under contract law, based on the contents of the agreement and the circumstances surrounding it, rather than by the agreement's title. The two types of settlement agreements are as follows.

(1) **Commutation.** A commutation settlement is a full-and-final or conditional settlement that sets aside settlement funds for future medical expenses and prescription drugs. Medicare payments for medical services for the work-related injury or illness will not be made by the federal government until the medical expenses disbursed by the primary payer related to the injury or illness are equal to the amount of the lump-sum payment.

Attorneys should always keep in mind that unless the commutation agreement specifically sets aside an amount for medical expenses, prescription drugs, lost wages, attorney's fees, and other expenses, and CMS approves the amount set aside in advance of the settlement, the entire lump sum amount may be deemed the liability of the primary payer for medical expenses. This ex-

posure creates "double liability" for the primary payer if CMS or the Medicare beneficiary files suit in federal court against the primary payer, as permitted by the MSP statute.

(2) **Compromise.** A compromise settlement agreement is one in which a lump sum of money is given in settlement of a workers' compensation claim. It does not admit liability by the insurer for a legally compensable injury.

As stated above, the MSP statute does not require an admission of liability by an insurer to impose liability for future medical benefits or grant CMS the authority to demand reimbursement for conditional payments. The insurer's settlement payment is the action which creates liability under the MSP statute. Payment of a settlement by an insurer automatically establishes liability as a primary payer.

Again, CMS realizes workers' compensation parties may seek to shift the costs of future medical benefits onto Medicare. As a result, if a settlement agreement allocates liability to an insurer only for past medical treatment, parties should be aware CMS will not automatically assume it is a compromise agreement.

If the facts of the case are such that it is clear the claimant will continue to seek medical treatment after the date of the settlement, the workers' compensation insurer will remain the primary payer. This is true even when the settlement agreement specifically attempts to terminate the insurer's liability for future medical treatment and the agreement does not provide for an insurer's liability for future medical expenses.

If it is clear at the time of settlement that the work-related injury or illness will create a continued need for medical care, then the agreement will not be a compromise settlement; it will be considered a commutation settlement. The workers' compensation insurer will remain the primary payer on the claim.

Furthermore, unless CMS approves of the allocation of indemnity benefits or attorney's fees, the entire settlement amount may be deemed available for payment of past or future Medicare-covered services related to the injury. The primary payer should not attempt to shift costs onto Medicare by closing medicals or transferring the burden onto Medicare, as CMS would then assert liens for double the amount of CMS's estimation of the appropriate amount that should have been set aside.

#### CMS RECOMMENDS OBTAINING APPROVAL PRIOR TO SETTLEMENT

A Workers' Compensation Medicare Set-Aside Arrangement ("WCMSA") is an allocation of funds from a final workers' compensation settlement used to pay for a claimant's future medical expenses and future prescription drug costs causally related

to the work injury or illness. A WCMSA is not necessary when resolution of the workers' compensation claim leaves the medical aspects of the claim open because the primary payer continues to have liability for future medical expenses and Medicare's interests will remain protected as a secondary payer.

A WCMSA may be submitted to CMS for review in the following situations:

- (1) The claimant is currently a Medicare beneficiary AND the total settlement amount is greater than \$25,000.00; OR
- (2) The claimant has a "reasonable expectation" of Medicare enrollment within 30 months of the settlement date and the anticipated total settlement amount for future medical expenses and disability/lost wages over the life or duration of the settlement agreement is expected to be greater than \$250,000.00. Existence of any of the five following factors is sufficient to establish "reasonable expectation":
  - (a) the claimant has applied for Social Security Disability Benefits;
  - (b) the claimant has been denied Social Security Disability Benefits but anticipates appealing the decision;
  - (c) the individual is in the process of appealing and/or re-filing for Social Security Disability Benefits;
  - (d) The claimant is sixty-two (62) years and six (6) months old (because then in thirty (30) months he will be eligible for Medicare based on the sixty-five (65) year age requirement); or
  - (e) the claimant has an End Stage Renal Disease ("ESRD") condition but does not yet qualify for Medicare based upon ESRD.

#### MANDATORY REPORTING REQUIREMENT EFFECTIVE JULY 1, 2009

The most recent legislation passed by Congress is the implementation of the MSP Mandatory Reporting Provisions in Section 111 of the Medicare, Medicaid, and SCHIP Extension Act of 2007 ("MMSEA").

Section 111 of the MMSEA adds new mandatory reporting requirements for group health plan ("GHP") arrangements and for non-GHP plans, including liability insurance, no-fault insurance, and workers' compensation insurance. The insurer's reports are to be submitted with respect to only Medicare beneficiaries (including a deceased beneficiary if the claimant was deceased at the time of the settlement, award, judgment, or other payment).

As it applies to workers' compensation claims, these changes only add reporting rules and do not eliminate any existing statutory provisions or regulations. They also include penalties for non-compliance. The penalty imposed by CMS for each Medi-

care beneficiary claimant whose workers' compensation claim is not reported will be \$1,000.00 a day.

Reports will be due in a specific form and manner, due after the claim is resolved, and in electronic format. The testing period for workers' compensation reporting begins July 1, 2009 and ends September 30, 2009. The first production files will be due between October 1, 2009 and December 31, 2009. All liability/no-fault/workers' compensation Responsible Reporting Entities ("RREs") will be required to submit production files by January 1, 2010.

#### RISKS ALL PARTIES TO A WORKERS' COMPENSA- TION CLAIM INVOLVING A MEDICARE BENEFICIARY SHOULD CONSIDER

In addition to the specific requirements set forth by CMS, all parties involved in workers' compensation claims should be aware that other issues have arisen as a result of this constantly changing area of law. These risks are discussed in depth below and include (1) the double liability of the primary payer if a claimant fails to reimburse Medicare for conditional payments made prior to the settlement, (2) the double liability of the primary payer if the expenditure for medical treatment has not been properly documented, (3) issues arising from the ambiguity in the law, (4) long delays and increased costs, (5) ambiguity in setting reserves, and (6) the risk of inflated settlement demands or a claimant's unwillingness to resolve his workers' compensation claim.

First, parties to workers' compensation claims must always manage their records properly and keep track of conditional payments made by Medicare prior to the date of the settlement or other payment. Conditional payment amounts can be requested directly from CMS. However, it is a more efficient rule of thumb if claimants and workers' compensation insurers work together to identify the payments disbursed for medical treatment and prescription drugs causally related to the work injury or illness.

If Medicare makes a conditional payment, and later believes a settlement agreement did not properly protect its interests, CMS may demand reimbursement for the conditional payment from the claimant, or if the claimant already spent the funds, from the primary payer, even if the primary payer had already paid that amount once to the claimant. This double liability imposed upon the primary payer is a serious risk for insurers.

Second, the primary payer can again have double liability related to the mismanagement of funds and documentation. If CMS approves a settlement arrangement and the funds set aside by the arrangement are exhausted, Medicare will then cover the costs of the claimant's future medical treatment and prescription drugs.

The primary payer's expenditures for causally related medical treatment and prescription drugs should be well documented because Medicare will not pay for any services directly related to the injury or illness until the beneficiary presents medical invoice amounts, in accordance with the Maryland Fee Schedule, that total the amount of the lump sum payment in a commutation settlement.

Third, another risk to consider is the ambiguity of the law. Due to the relatively recent enactment of many of these laws, CMS' past inability to pursue every claim in a timely and effective manner, and the long process of exhausting administrative remedies, many issues that workers' compensation parties have tried to resolve have yet to be addressed by the federal courts.

One example of an ambiguity in the law that has not yet been addressed by federal appellate courts is the seemingly contradictory fact that CMS will not recognize a settlement that shifts the cost from the primary payer to Medicare, but CMS may approve a lump sum compromise settlement arrangement, which relieves the primary payer of all medical expenses incurred after the date of the settlement. The argument is that any settlement with closed medicals may be considered cost-shifting from the primary payer to Medicare.

Fourth, there is a risk that there are long delays associated with the settlement of workers' compensation claims created by the CMS approval process. Both the approval process and the new mandatory reporting requirements also lead to increased costs associated with compliance with the MSP statute.

Workers' compensation is a system specifically structured to allow speedy payment to injured workers, and Maryland has one of the most efficient systems in the country. As such, the longer the delay in obtaining approval of a settlement arrangement, the longer a claimant must wait for compensation benefits. This, in turn, also amounts to increased litigation costs for the primary payer. The multi-step process requiring CMS' review of settlement arrangements threatens the efficient functioning of the workers' compensation system. The delay is caused by the collection of medical records and invoices, determination of Medicare lien amounts, cost estimation and allocation, review by the recovery contractor assigned by CMS, and determination of the existence of prior liens.

The mandatory reporting requirements effective July 1, 2009 create a new burden for the workers' compensation insurers who can only file their reports electronically. The electronic submission requirements increase the costs associated with all workers' compensation claims involving Medicare beneficiaries. These costs are irrespective of whether the claim is ever resolved. The only

requirement is that the claimant must also be currently entitled to Medicare benefits.

Fifth, the ambiguity of laws creates risk. The potential for an insurer's double liability, and the new but steep penalty liability will make it difficult for primary payers to effectively set reserves and properly plan for future liability on workers' compensation claims. Accordingly, insurers are faced with the difficult task of setting reserves on these types of cases.

CMS both has the option and lacks the resources to make a demand for reimbursement of conditional payments in all workers' compensation cases. If CMS does make a demand, no formula for reimbursement exists. As such, it is not clear what method of calculation is employed by CMS to determine the amount of its anticipated demands for reimbursement.

Yet another obstacle is created in the reimbursement demand process by the relatively long federal statute of limitations period. The primary payer must wait up to six years to determine if CMS will ever issue a reimbursement demand letter on a claim. And, the only way to determine the amount of the reimbursement liability to CMS is by receiving the demand letter.

Furthermore, the federal courts have held that they will not order CMS to provide a final reimbursement demand because a claimant must first exhaust his administrative remedies. This means the insurer must remain waiting for up to six years to determine if CMS will issue a demand letter at all, and if so, for what amount.

The primary payer's liability exposure to Medicare remains open on a claim if future medical treatment has not been closed in the settlement agreement. In Maryland, there is no limitations period for future medical treatment on a workers' compensation claim. So, although an insurer effectively deems a claim closed, the potential liability for future medical treatment remains open until a full and final settlement has been approved by the Maryland Workers' Compensation Commission.

Sixth, the new liabilities of claimants, primary payers, and attorneys create another risk: inflated settlement demands from claimants or the plain unwillingness to settle. Medicare does not recognize medical and non-medical portions of settlement arrangements. In cases of compromise of liability, this system allows claimants to push for unjustified settlement amounts. This may occur because employers will agree to a settle in a case where liability has not been fully established.

As a result, the amount of future medical expenses may be greater than the amount the primary payer offers to settle. Al-

though a primary payer's liability for a settlement arrangement approved in advance by CMS is capped at the amount specifically allocated for future causally related medical expenses, attorneys on both sides of the workers' compensation claim will have to confront this issue head-on during settlement negotiations. This potential future liability is another obstacle to settlement created by the MSP statute and may prolong and deter negotiations all together.

It is also important to note another hindrance to the settlement of a workers' compensation claim. CMS will not participate in pre-settlement negotiations. This will probably further delay or prevent an agreement. Attorneys may wish to avoid all of the ambiguities and difficulties with this system and choose not to settle the case.

But, parties should keep in mind that Medicare may still have interests in any award, judgment, or other payment besides a final agreement of compromise and settlement. Additionally, as a result of the new mandatory reporting requirements, CMS will have notice of which primary payers continue to have primary payer liability for future medical treatment as a result of a work-related injury or illness sustained by current Medicare beneficiaries.

#### FEDERAL HOLDINGS

The MSP statute casts Medicare as the secondary payer in virtually all situations if any other insurance coverage exists. This creates a cause of action for Medicare to seek reimbursement from primary payer insurance funds. The federal government has standing to intervene in litigation between the beneficiaries and primary payers when the primary payer is disputing the beneficiary's claim. Several of the holdings of federal appellate courts involving issues related to the MSP statute follow.

#### MEDICARE HAS NO RIGHT OF REIMBURSEMENT FROM AN UNINSURED EMPLOYER THAT SETTLES A WORKERS' COMPENSATION CLAIM

The United States Court of Appeals for the Fifth Circuit held a party that settles a Medicare recipient's claim against it is not, *ipso facto*, a "self-insurer" under the MSP statute. *See Thompson v. Goetzmann*, 337 F.3d 489 (5th Cir. 2003). The payment by the primary payer must be made under a "primary plan" of self-insurance, which requires both an arrangement for (1) a source of funds, and (2) procedures for disbursing these funds when claims are made against the employer. *Id.* at 498.

The employer therefore, to be liable for reimbursement to Medicare, "would have to engage in the same sorts of underwriting procedures that insurance companies employ; estimating likely losses during the period, setting up a mechanism for creating sufficient reserves to meet those losses as they occur,

and, usually, arranging for commercial insurance for losses in excess of some stated amount." *Id.* A plan must be in place as an arrangement to provide health benefits or assume legal liability. *Id.*

Accordingly, an uninsured employer that settles a Medicare beneficiary's workers' compensation claim would not be liable to Medicare for reimbursement of prior conditional payments or future medical expenses. The primary payer identified under the federal statutes must be an insurance company or a self-insurer structured like an insurance company.

An uninsured employer, that under Maryland law would be liable to a claimant for an accidental injury or occupational disease, would not be liable for reimbursement to Medicare. CMS does not have the reach to demand reimbursement from any party in a workers' compensation case if the payment to the claimant was not made under a "primary plan." *Id.* at 503. The claimant and the attorneys in the case would also, as a result, have no reimbursement liability to Medicare.

It is important to note, however, Goetzmann applauded the federal government for its motive in seeking to recoup funds it had disbursed for Medicare treatment and services. *Id.* It also advised that the desire to expand the list of those responsible for reimbursement should be directed to Congress rather than the courts. *Id.* In light of the many changes to the MSP program in the past several years, this is a change which may be fast approaching fruition.

#### MEDICARE IS NOT ENTITLED TO DOUBLE DAMAGES AGAINST RECIPIENT OR HIS ATTORNEY

Workers' compensation attorneys should be relieved to know that although they are liable for protecting Medicare's interests, they are not liable for double damages to Medicare. Payment by Medicare is conditional when payment has been or can reasonably be expected to be made under an insurance policy.

If Medicare is not reimbursed for conditional payments by the beneficiary, the primary payer must reimburse Medicare even though it has already reimbursed the beneficiary or other party. *U.S. v. Sosnowski*, 822 F.Supp. 570, 573, 41 Soc.Sec.Rep.Serv. 312, Med & Med GD (CCH) P 41,068 (W.D. Wisc. 1993). The Court held double damages were not appropriate in that case because neither the Medicare beneficiary nor his attorney were a "primary plan" and double damages are only available when a primary plan fails.

#### CMS MAY RECOVER UP TO THE FULL AMOUNT OF CONDITIONAL MEDICARE PAYMENTS EVEN WHEN THE BENEFICIARY RECEIVES A DISCOUNTED THIRD

## PARTY SETTLEMENT

Often another issue in workers' compensation settlements is the workers' compensation insurer's subrogation lien against a third party liability insurer. This occurs when a claimant is entitled to workers' compensation benefits under Maryland workers' compensation law, but is also entitled to damages as a result of a third party tortfeasor's negligence. In Maryland, workers' compensation insurers have an automatic lien against those third party liability insurers for the amount of medical and indemnity payments made on the claim.

The subrogation provisions of the MSP statute give the federal government the right to be put in the legal position of the Medicare beneficiary in order to recover from third parties who are legally responsible for the beneficiary for a loss. *Zinman v. Shalala*, 67 F.3d 841, 844, 49 Soc.Sec.Rep.Serv. 128, Med & Med GD (CCH) P 43,653 (9th Cir. 1995). *Zinman* rejects the principle that because the right of subrogation is equitable in nature, a subrogated right holder is limited to recovery of the proportion of its loss for which third-party reimbursement is actually received.

Instead, *Zinman* holds the MSP statute allows full reimbursement of conditional Medicare payments even though a beneficiary receives a discounted settlement from a third party. *Id.* at 845. "The transformation of Medicare from the primary payer to the secondary payer with a right of reimbursement reflects the overarching statutory purpose of reducing Medicare costs." *Id.*

The Court made a point to reject an equitable apportionment of third party settlements because, it opined, workers' compensation cases are different than tort cases. *Id.* at 846. Workers' compensation schemes generally determine recovery on the basis of a rigid formula, often with a statutory maximum. *Id.* Apportionment in workers' compensation settlements is relatively simple to calculate. *Id.*

"Tort cases, in contrast, involve noneconomic damages not available in workers' compensation cases, and a victim's damages are not determined by an established formula." *Id.* The Court refused to find that Medicare's recovery amount from a tort liability settlement should require a factfinding process or be "at the mercy of a victim's or personal injury attorney's estimate of damages." *Id.*

## A THIRD PARTY LIABILITY INSURER SATISFYING A WORKERS' COMPENSATION SUBROGATION LIEN MAY BE LIABLE FOR DOUBLE DAMAGES

The MSP statutory provisions also apply if a third party payer makes its payment to an entity other than Medicare when it is, or should be, aware that Medicare has made a conditional primary payment. *Sosnowski*, 822 F.Supp. at 573. This holding is especially relevant to workers' compensation claims that involve third

party liability. CMS, in that type of case, would be entitled to demand reimbursement for payments from the third party liability insurer, even if the third party had satisfied the workers' compensation insurer for the full amount of the subrogation lien.

## A PRIVATE CITIZEN MAY COLLECT DOUBLE DAMAGES BY BRINGING CLAIMS AGAINST PRIMARY PAYERS TO RECOVER MONEY OWED

A noteworthy case involving an accepted claim for an occupational disease under Maryland workers' compensation law visits a provision of the MSP statute which allows private citizens to collect double damages by bringing claims against primary payers to recover money owed to Medicare. *O'Connor v. Mayor and City Council of Baltimore*, 494 F.Supp.2d 372, Med & Med GD (CCH) P 302,166 (D. Md. 2007). The district court held the claimant had standing to bring the claim for double damages because an injury in fact had occurred, a causal connection had been established between his disease and his employment, and a decision in his favor would redress his injury. *Id.* at 374.

Unfortunately, like many other issues created by the MSP statutes, no other opinion has been drafted by any Federal court regarding the issues raised by Medicare beneficiary and workers' compensation claimant O'Connor. However, the *O'Connor* opinion, through dicta, indicates that the federal courts in our jurisdiction will not hesitate to enforce the MSP provisions imposing liability upon primary payers.

## CONSULTANTS THAT ASSIST IN STRUCTURING WORKERS' COMPENSATION SETTLEMENT ARRANGEMENTS MAY HAVE STANDING TO BRING SUIT AGAINST THE FEDERAL GOVERNMENT

Consulting companies often assist parties to workers' compensation claims in structuring settlement arrangements that comply with CMS regulations designed to assure that Medicare's interests are considered when the claimants are persons eligible for Medicare benefits. These consulting companies typically receive a fee from the settlement proceeds. *Protocols, LLC v. Leavitt*, 549 F.3d 1294, Med & Med GD (CCH) P 302, 685 (10th Cir. 2008).

Protocols filed suit against the Secretary of the Department of Health and Human Services and the Acting Administrator of CMS alleging that a memorandum issued by CMS misinterpreted the MSP statute and regulations and exposed Protocols to unexpected liabilities arising out of settlements it had structured in the past. *Id.* at 1294.

Protocols alleged a change in the law by CMS would create liability for the company as a result of CMS' potential refusal to recognize prior settlements. This, Protocols alleged, would lead to a decrease in the company's value, uncertainty of how much revenue it must not use for capital or operating costs in case of

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future exposure, and postponed discussions with potential investors awaiting the outcome of the lawsuit.

The Court found that these reasons did amount to injury in fact, and therefore Protocols had standing to bring suit against the federal government. This case reaffirms that the liabilities imposed by the MSP statute affect all parties to workers' compensation claims, not just claimants and insurers.

#### A CLAIMANT MUST EXHAUST HIS ADMINISTRATIVE REMEDIES TO RECOVER ON ANY CLAIM ARISING OUT OF THE MEDICARE ACT

The Medicare statute requires that any lawsuit which seeks to recover on any claim arising under it must first be brought through the Department of Health and Human Services administrative appeals process before it can be filed in federal court. *See Walters v. Leavitt*, 376 F.Supp.2d 746, Med & Med GD (CCH) P 301,666 (E.D. Mich. 2005). The Medicare beneficiaries in this case filed suit to compel CMS to produce the itemized list of federal Medicare benefits paid on their behalf, including the reimbursement amount Medicare will seek. *Id.* at 749.

The district court held the beneficiaries had made no attempt to exhaust their administrative remedies and they can obtain precisely the information they seek by following the administrative process outlined by CMS. *Id.* at 755.

The administrative process begins with a request to CMS. *Id.* at 756. If CMS denies the request, the party would then seek review of that denial at a hearing before an administrative law judge. *Id.* If still unsatisfied, the party should request review of the administrative law judge decision by the Department of Health and Human Services Appeals Board. *Id.* If the party again receives an unfavorable decision, filing a claim in Federal court is then proper. *Id.*

This long line of administrative procedures acts as a deterrent for litigation of issues raised by enactment of the MSP statute. The associated litigation costs are another serious risk to consider when determining liability arising from a workers' compensation claim.

#### CONCLUSION

In light of the evolving federal laws involving Medicare beneficiaries entitled to future medical treatment and prescription drugs under a workers' compensation primary payer insurance plan, no party to a workers' compensation claim can afford to ignore the liabilities imposed.

The newly enacted penalties for the failure to report Medicare beneficiaries entitled to continued medical treatment under a

primary payer plan to CMS have effectively ended the days in which all parties to workers' compensation claims may have been able to afford non-compliance with the MSP program. CMS will soon have the ability to determine if a workers' compensation insurer is liable for payments for a Medicare beneficiary's medical payments. The anticipated result is an increase in the number of demands for reimbursement for conditional payments made by Medicare.

## Relief for Employers Hoping to Avoid Layoffs During Difficult Economic Times

*By Christina Bolmarcich*

According to the U.S. Bureau of Labor and Statistics, the unemployment rate has soared to 8.1%, the highest in twenty-five (25) years. Often people view a layoff as a hardship only for employees because of the economic burdens they will face. However, layoffs are often challenges for employers, who are left with lower worker morale, and the inability to maintain a professional level of productivity necessary to operate their businesses.

For employers seeking a solution to the layoff dilemma, the Maryland General Assembly passed legislation which established the Work Sharing Unemployment Insurance Program.<sup>1</sup> This program allows employers to reduce employees' hours by the same percentage while maintaining its entire workforce. It also allows employees to receive unemployment benefits for a maximum of twenty-six (26) weeks in a benefit year without the strict conditions imposed on them when collected regular Unemployment Insurance.

The benefits of the Work Sharing Program for employers include permitting an employer to maintain its business, keep employee morale high, and avoid rehiring and retraining new or additional employees when financial times improve. For employees, the benefits allow them to maintain a sense of belonging and avoid the negative financial burden that they would have faced should they have been the victim of a total layoff.

To participate in the Work Sharing Program, an employer does not have to apply the reduction in hours to all employees throughout its organization. In contrast, the employer can apply the reduc-

tion to an entire affected department, shift, or unit so long as it is comprised of two or more employees. To qualify, an employee must have been on the payroll continuously for at least three months, and may not be a part-time employee.

The Work Sharing Program is codified in Sections 8-1201 through 8-1208 of the Maryland Annotated Code. The general procedure for an employer to participate is as follows:

- (a) The employer shall submit written work sharing plan Secretary of Labor, Licensing, and Regulation.<sup>2</sup>
- (b) A work sharing plan shall apply to at least ten percent or at least twenty (20) employees in a specific plant, department, shift, or other definable employing unit.<sup>3</sup>
- (c) The normal weekly work hours of the affected employees shall be reduced by at least ten percent, unless waived by the Secretary of Labor, Licensing, and Regulation, but may not exceed fifty percent.<sup>4</sup>
- (d) The work sharing plan shall identify the affected employees by name, Social Security number, and any other information that the Secretary of Labor, Licensing, and Regulation may require.<sup>5</sup>
- (e) The work sharing plan must specify an expiration date that is not more than six months the effective date of the work sharing plan.<sup>6</sup>
- (f) The work sharing plan must specify the fringe benefits of each named employee including, but not limited to, health insurance benefits, retirement benefits, and sick leave benefits.<sup>7</sup>
- (g) The work sharing plan shall certify that each named employee has been continuously on the payroll of the specific plant, department, shift, or other definable employing unit for at least three months and that the reduction in normal working hours is instead of layoffs.<sup>8</sup>
- (h) If an employer participates in a collective bargaining agreement, the union bargaining agent's or employee representative's consent must accompany the work sharing plan.<sup>9</sup>
- (i) If the work sharing plan serves the employer as a transitional step to permanent staff reduction, the work sharing plan shall contain a reemployment assistance plan for each named employee.<sup>10</sup>
- (j) The employer shall submit reports to the Secretary of Labor, Licensing, and Regulation that are necessary for administration of the work sharing plan.<sup>11</sup>

For lawyers representing employers in the process, the Maryland Annotated Code sets out the requirements for the eligibility of employees and how benefits are determined.<sup>12</sup> The Work Sharing Program may be a great solution for employers during the present difficult economic time. For more information or the requirements for participation, visit [www.dllr.state.md.us](http://www.dllr.state.md.us).

Footnotes:

- <sup>1</sup> Md. Code Ann., Lab. & Empl. § 8-1201 through § 8-1208 (2008).
- <sup>2</sup> *Id.* at §8-1203(a).
- <sup>3</sup> *Id.* at §8-1204(1).
- <sup>4</sup> *Id.* at §8-1204(2).
- <sup>5</sup> *Id.* at §8-1204(3).
- <sup>6</sup> *Id.*
- <sup>7</sup> *Id.*
- <sup>8</sup> *Id.*
- <sup>9</sup> *Id.*
- <sup>10</sup> *Id.* at §8-1204(4).
- <sup>11</sup> *Id.* at §8-1204(5).
- <sup>12</sup> *Id.* at §8-1206 and §8-1207.



## **REMINDER:**

*The Labor & Employment Law Section of the  
Maryland State Bar Association presents:*

### **Brown Bag Luncheon EEOC Administrative Judges Open Forum**

Join the Administrative Judges of the Equal Employment Opportunity Commission Baltimore Field Office for a brief presentation on Federal Employment Discrimination Law and administrative procedures followed by a question and answer session. This is your opportunity to ask the judges questions about office procedures, case processing and substantive law.

**Date:** Wednesday, May 6, 2009

**Time:** 12:00 noon to 2:00 p.m.

**Place:** EEOC, 4th Floor Conference Room,  
10 South Howard St., Baltimore, MD 21201

*(Drinks and cookies will be provided)*

#### Administrative Judges:

Laurence Gallagher

Enechi Modu

David Norken

Charles Shubow

#### Chief Administrative Judges:

Mary Elizabeth Palmer

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